

Exhibit 37. Network Affiliation Balance for Top 25 Broadcasters

Broadcaster	Total "Syndicator" Clearance	Percent Clearance ABC	Percent Clearance CBS	Percent Clearance NBC	Percent Clearance Fox	Percent Clearance UPN	Percent Clearance WB	Percent Clearance Independent
Paxson Communications	57.1%	2.6%	0.0%	0.0%	0.9%	0.0%	0.0%	96.5%
News Corp. (Fox Broadcasting)	40.4%	0.0%	0.0%	0.0%	100.0%	0.0%	0.0%	0.0%
Tribune	35.6%	1.8%	4.8%	0.0%	15.6%	0.0%	77.8%	0.0%
CBS Corp.	31.8%	0.0%	100.0%	0.0%	0.0%	0.0%	0.0%	0.0%
USA Networks, Inc.	31.0%	0.0%	0.0%	0.0%	0.3%	0.0%	0.0%	99.7%
General Electric (NBC)	27.3%	0.0%	0.0%	100.0%	0.0%	0.0%	0.0%	0.0%
Univision Communications	27.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	100.0%
Disney (ABC)	24.2%	100.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Viacom	23.8%	0.0%	0.0%	0.0%	0.0%	95.9%	4.1%	0.0%
Sinclair Broadcast	22.4%	18.6%	5.1%	3.3%	45.4%	1.0%	15.0%	11.6%
Chris-Craft Industries (BHC, United)	21.6%	3.3%	0.0%	3.1%	0.0%	89.0%	0.0%	4.7%
Telemundo Group	21.5%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	100.0%
Gannett Broadcasting	16.3%	7.0%	29.0%	64.1%	0.0%	0.0%	0.0%	0.0%
A.H. Belo	14.2%	30.4%	34.9%	28.1%	6.6%	0.0%	0.0%	0.0%
Raycom	10.2%	9.9%	35.5%	26.9%	25.5%	2.2%	0.0%	0.0%
Scripps Howard	9.8%	80.7%	0.0%	19.3%	0.0%	0.0%	0.0%	0.0%
Cox Enterprises	9.5%	38.4%	21.8%	12.3%	27.6%	0.0%	0.0%	0.0%
Young Broadcasting	9.2%	30.5%	10.4%	3.4%	0.0%	0.0%	0.0%	55.7%
Hearst-Argyle Television	8.9%	73.7%	0.0%	26.3%	0.0%	0.0%	0.0%	0.0%
Glencair Acquisitions	8.5%	0.0%	0.0%	0.0%	23.4%	19.5%	41.9%	15.3%
Meredith	7.7%	0.0%	45.8%	10.5%	43.7%	0.0%	0.0%	0.0%
Washington Post	7.1%	29.1%	22.1%	48.8%	0.0%	0.0%	0.0%	0.0%
Granite Broadcasting	7.0%	15.7%	12.1%	12.9%	0.0%	0.0%	59.3%	0.0%
All-American TV, Inc.	6.8%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	100.0%
Clear Channel	6.2%	10.2%	19.0%	7.5%	57.4%	5.9%	0.0%	0.0%

Source: Bear, Stearns and Co. Inc. estimates; Nielsen Media Research; BIA Investing in Television '97.

Geographic Balance Is a Natural Hedge

We believe that a station group should work toward a strong geographic balance, as this helps reduce reliance on any particular market or regional economy. Exhibit 38 summarizes the geographic profile of the six public television broadcasters on which we have recently initiated coverage.

Exhibit 38. Geographic Balance of Largest Broadcasters

Regional Distribution (Percent)	A. H. Belo	Granite Broadcasting	Hearst-Argyle Television	Sinclair Broadcast	USA Networks	Young Broadcasting
Northeast	0.0%	14.7%	53.0%	18.6%	38.1%	5.7%
South	52.6%	6.5%	12.8%	33.9%	29.9%	21.1%
Midwest	8.0%	35.1%	27.5%	40.4%	15.5%	17.5%
West	39.4%	43.7%	6.8%	7.2%	16.5%	55.7%
Totals	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%

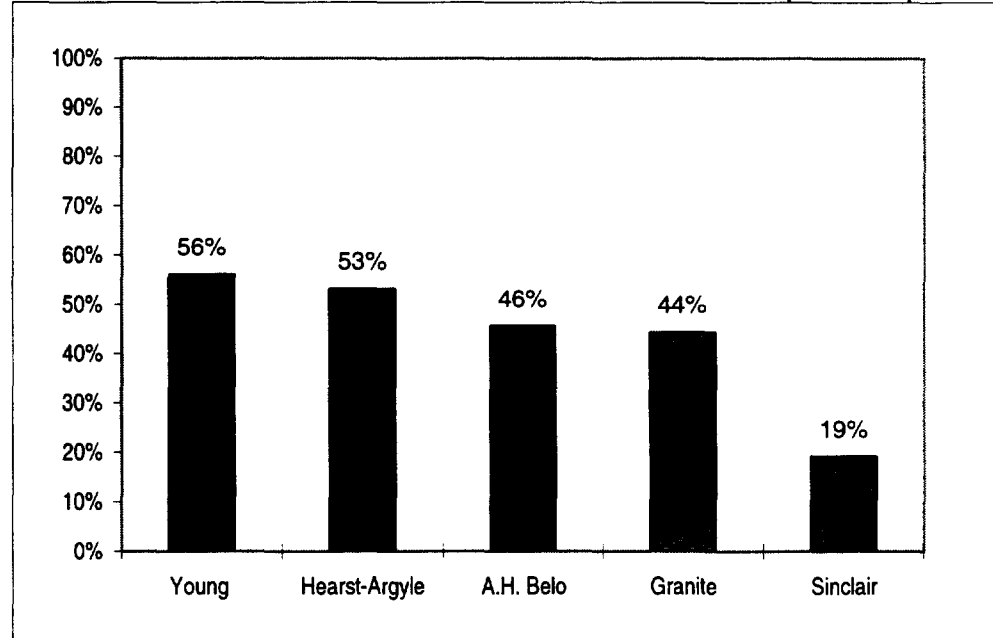
Source: Nielsen; Bear, Stearns and Co. Inc.

Diversified Sources of Cash Flow Lowers Risk

In our view, a well-diversified portfolio of strong cash flow-producing properties is one of the television broadcaster's best defenses against the vagaries of the business cycle and changes in regional economics. While we do not have cash flow estimates for each of the properties owned by the five public companies highlighted in this report (excluding USA Broadcasting, which plans to convert its television properties to commercial stations beginning in June 1998), we have devised revenue estimates for each. In Exhibit 39, we show the projected percentage of revenues earned by the

three largest properties for each of these five broadcasters. According to this measure, Sinclair Broadcast Group is the least reliant on its three largest properties and, thus, has the best overall balance in cash flow sources in the group. (We've omitted USA Broadcasting, an operating unit of USA Networks, Inc., because its stations have not yet undergone their transition from Home Shopping Network affiliates to independent broadcast stations.)

Exhibit 39. Estimated Revenue Concentration of Selected Broadcaster's Top Three Properties



Source: BIA Investing in Television '97; Bear, Stearns and Co. Inc.

CONTROL FACTOR NO. 4: A DUAL-MEDIA PRESENCE

In our view, broadcasters that have forged a dual-media presence — e.g., owning television and radio properties, television and outdoor advertising assets, and/or television and cable networks; program and sell advertising for two television stations (through local marketing agreements); or own television and newspapers (through grandfathering of laws) in the same market — will enjoy significant competitive and economic advantages over local rivals that have not done so.

Advantages of Ownership of Multiple Media in a Local Market

Advantages of multiple-media ownership in a local market include:

- the ability to cross-promote local media properties;
- the ability to offer local advertisers a choice between two local advertising mediums;
- the ability to gain a higher profile with local advertisers (local advertising is becoming much more important television and is the dominant share of advertising in radio);
- the ability to provide advertising packages;

- the ability to leverage the salesforces more effectively; and
- the ability to create programming and cost efficiencies by extending franchise of one media entity into another — i.e., by using the journalistic force of a newspaper to enhance news programming on the local television station or using radio formats that are most suitable for the TV station's viewer demographics.

Advantages of Operating Two Local TV Stations

In addition, we believe that the effective management of two television properties in the same market can create interesting possibilities. These combinations are usually formed between an owned and operated local station and a local marketing agreement. They also typically involve the linkage of two emerging networks (Fox/WB, Fox/UPN, or WB/UPN) or the combination of an affiliate and a pure independent (not affiliated with any network) station. LMAs are formed when one local operator pays another operator in the same market for the right to program and sell the advertising inventory of that station. This ownership setup gives the station group the ability to:

- offer local advertisers a choice between two television properties;
- compete more effectively against the Big Three (ABC, CBS, and NBC) network-affiliated television properties in the market;
- duplicate the favorable cash flow economics enjoyed by larger local network affiliates by diversifying revenues streams;
- leverage the salesforce more effectively;
- enjoy greater influence with program suppliers in the local market;
- make it easier for a broadcaster to promote and pay for having a local market "metered," which generally leads to increased ratings for traditional independent television properties (now Fox, WB, and UPN affiliates);
- increase the likelihood that advertisers will spend some part of their ad budgets on the company's stations; and
- increase its profile with local advertisers;
- launch a new news product on the LMA-ed

In Exhibit 40, we summarize the TV/radio, TV/TV, and TV/newspaper cross-ownership relationships of select broadcasters.

Exhibit 40. Cross-Ownership of Select Public Broadcasters

Cross-Ownership Opportunity	A. H. Belo	Granite Broadcasting	Hearst-Argyle	Sinclair Broadcasting	USA Networks	Young Broadcasting
TV-LMAs/Minority Interest	Seattle Honolulu Spokane Tuscon	None	Kansas City Tampa West Palm Beach	Pittsburgh Baltimore Indianapolis Raleigh-Durham Milwaukee Nashville Asheville, NC San Antonio Oklahoma City Greensboro Birmingham Dayton Charleston Mobile-Pensacola Syracuse Paducah Charleston, SC Las Vegas, NV Columbus, OH Tyler	Chicago San Francisco Washington Denver St. Louis	None
TV-Radio	None	Buffalo	Baltimore	St Louis Milwaukee Kansas City Norfolk Greenville Buffalo Greensboro	None	None
TV-Newspaper	Dallas	None	None	None	None	None
Cable Networks	Northwest Cable News Texas Cable News	None	None	None	USA Network Sci-Fi Network Home Shopping Network	None

Source: *Broadcasting & Cable*; Federal Communications Commission; BIA Investing in Television '97; company reports; Bear, Stearns & Co. Inc.

We believe that the consolidation currently taking place in the industry could accelerate further if:

- the one-to-a-market rule, which restricts the number of television and radio properties one broadcaster can own in a single market, is eliminated (which we think is quite possible);
- local marketing agreements are permitted going forward (which we think could be codified to consider the terms entered into between the LMA and its operating partner and the impact on local viewership choices and separate owners (i.e., "voices"); or

- duopolies are permitted in television, allowing an operator to own two television properties in the same market (which we believe is highly unlikely at this time).

We expect that many television rulemakings, which have been under review at the FCC for the past several years, are likely to be decided by the third quarter of 1998. In the long term, we believe that duopolies may ultimately be allowed, spurred by the reality of a progressively competitive video marketplace.

One-to-a-Market Rule Could Be Relaxed or Eliminated

The fate of the one-to-a-market rule (OMR) may be determined by the FCC as part of the November 1996 Second Notice of Proposed Rulemaking, which addresses attribution, local ownership, and cross-ownership issues. The OMR currently permits an operator in the top 25 markets to own one television station, one FM radio station, and one AM radio station in the same market. The upcoming rulemaking is likely to extend the OMR to the top 50 markets and could raise the radio station limit to two AM and two FM stations. However, the rulemaking also contemplates the total elimination of the OMR, which has been liberally waived to permit broadcasters to own more than one FM and one AM station in a market in cases when they also own a television station. A significant "test case" against the existence of the one-to-a-market rule is the fact that CBS/Westinghouse and Infinity were ultimately allowed to combine. Also, in scrutinizing radio deals, the Department of Justice has been focusing on operators' post-transaction share of radio advertising, arguing that radio revenue is distinct from other advertising forms. This view would actually support the disbanding of the OMR altogether. If this occurs, we believe the pressure for television and radio broadcasters to merge will increase dramatically.

Television Duopoly Is Unlikely; LMAs May Survive

As part of the Telecommunications Act of 1996, the FCC is expected to revisit local ownership rules in television. The FCC issued a Notice of Proposed Rulemaking in November 1996 and has received comments on proposed rule changes from industry players, government agencies, trade associations, and consumer advocacy groups. The FCC could address local ownership rules by the third quarter of 1998. We doubt that it will make any meaningful changes to the local ownership rules that would permit duopoly, for several reasons, listed below.

- The Clinton Administration, the Department of Justice (comments filed on the Proposed Rulemaking on May 16, 1997), and the Department of Commerce (comments filed on May 22, 1997) all oppose ownership changes.
- We doubt the FCC will confront the President on this issue.
- Although the FCC may have been willing to provide some duopoly relief as recently as two or three years ago, broadcasters within the television business were divided on the issue. For example, in adopting language to officially endorse duopoly two years ago, the National Association Board carried the resolution by a narrow 13-9 vote. Without a clear consensus within the industry, we think it is less likely that the FCC will act aggressively on the duopoly issue.

- To a certain extent, we believe that the rapid consolidation in the radio business may have hurt the prospects for ownership changes in the television broadcast industry at the FCC.

As we see it, the FCC is probably weighing its concerns about maintaining local market "voices" (i.e., distinct and separate broadcast owners) against the benefits of new "choices" created by the investment in stations through LMAs, which is the closest approximation to a duopoly that a television broadcaster can achieve. We think the FCC may ultimately permit ad hoc duopoly waivers to allow for the continuance of LMAs on a case-by-case basis. In most instances, we believe structures such as LMAs could survive, mostly because LMAs typically involve a particularly weak player in local market or a new station that recently signed on (which often requires the economic support of another broadcaster).

By our estimates, LMAs in the top 100 markets earn only 1.2% of all local TV ad spending and an average 3.5% and 4.0% in revenue and viewership share of local markets, respectively. As Exhibit 41 illustrates, 80% of all LMAs earn less than 5% revenue share and 5% viewership share, respectively.

Exhibit 41. Average Revenue Share and Viewership Share of LMAs

Revenue Percent	Number of LMAs	Percent Distribution	May 97 Viewing Share	Number of LMAs	Percent Distribution
0%-2.5%	33	47%	0	21	30%
2.6%-5.0%	18	26%	1	0	0%
5.1%-7.5%	6	9%	2	12	17%
7.6%-10.0%	4	6%	3	12	17%
10.1%+	9	13%	4	12	17%
Total	70	100%	5	3	4%
			6+	10	14%
				70	100%

Source: Bear, Stearns and Co. Inc. estimates.

If viewership and revenue share in a local market was low, the average station would probably not have been able to begin operation or continue operating without the assistance of a stronger, better-capitalized player. In addition, as Exhibit 42 illustrates, many LMAs support the emerging UPN and WB networks or pure independent stations (which are becoming rarer), and this increases viewership choices and creates more local competition.

Exhibit 42. Local Marketing Agreements — Affiliations

May Share	Number of LMAs	Percent Distribution
UPN	20	29%
WB	19	27%
Fox	9	13%
Independent	8	11%
Infomercial	3	4%
Home Shopping	2	3%
Big Three Affiliate (ABC, CBS, NBC)	7	10%
Dark	2	3%
Total	70	100%

Source: *Broadcasting & Cable*; Federal Communications Commission; BIA Investing in Television '97; company reports; Bear, Stearns & Co. Inc.

However, we still believe that the FCC may find that the public-interest advantages of having more viewership options may outweigh the potential narrowing of choices. Congress, as part of the negotiations in the 1998 budget bill, also weighed in on the

issue. In the manager's statement that accompanied the budget bill, Congress provided guidance to the FCC regarding LMAs and duopoly by encouraging the FCC to permit the permanent grandfathering of LMAs and to allow duopoly if it is in the public interest. As we stated earlier, despite these signs of prodding from Congress, we think it is highly unlikely that the FCC will make any substantive changes that would significantly loosen local ownership rules.

Most broadcasters have entered into LMAs that feature specific terms with the LMA-ed station. Perhaps the FCC could adopt rules that grandfather LMAs (to please Congress) until the contractual terms of the LMA have ended (the FCC may not want to materially improve the contracts into which local stations entered) and then review whether a local station should be able to renew the LMA arrangement based on the local competitive environment at that time. Such a review should take into account the emergence of digital television and the continued fractionalization of TV audiences, which we think would warrant a waiver at that time.

We believe that significant owners of LMAs, including Sinclair Broadcast Group, A.H. Belo Corp., and Clear Channel, may find relief in an ad hoc case-by-case duopoly waiver for the majority of their stations. Those that do not receive waivers (assuming they are "too viable" in the long run) could be sold or swapped, capturing significant value given today's M&A environment.

Exhibit 43. Local Marketing Agreement Summary in Top 100 Television Markets

Owner	Number of LMAs	LMA Revenues	Gross Market Revenues	Percent of Market Revenues
Sinclair Broadcasting	20	\$145,700	\$2,051,500	7.1%
Clear Channel	8	\$31,500	\$591,800	5.3%
LIN Television	5	\$25,600	\$878,200	2.9%
A.H. Belo	4	\$6,500	\$450,300	1.4%
Paxson Communications	2	\$3,200	\$667,300	0.5%
NBC	2	\$4,500	\$237,400	1.9%

Source: *Broadcasting & Cable*; Federal Communications Commission; BIA Investing in Television '97; company reports; Bear, Stearns & Co. Inc.

CONTROL FACTOR No. 5: DEBT CAPACITY/FINANCIAL FLEXIBILITY

In a consolidating industry, television broadcasters must have a flexible capital structure and borrowing capacity. Operators with heavy debt burdens are limited in their ability to make acquisitions. However, many broadcasters have been able to repeatedly tap the capital markets in order to pay down debt and have sufficiently gained the confidence of the investment community to access capital quickly. Moreover, the multiples accorded the equities of various broadcasters also provide advantages, especially for those that use their stocks as acquisition currency to bid more aggressively for properties — recognizing that the stock will be an important part of the transaction and/or that, if necessary, additional equity could be raised at an attractive multiple. In Exhibit 44, we analyze the capital structures of the broadcasters on which we have launched research coverage from two vantage points — debt capacity and the value of a company's currency (stock).

- **Debt Capacity.** We first calculated each broadcaster's current leverage, using this figure to ascertain its acquisition capacity given a maximum target debt level of 6.5x operating cash flow and various purchase multiples.

- **Current Trading Multiples.** We also compared each broadcaster's current share price multiples in order to get a sense of a stock's value as an acquisition currency. Obviously, the stocks with higher trading multiples have two advantages — they can bid more aggressively for properties, and they are less likely to do dilutive deals.

Exhibit 44. Flexibility of Capital Structure of Publicly Traded TV Operators

	A. H. Belo	Granite Broadcasting	Hearst Argyle Television	Sinclair Broadcast Group	USA Networks	Young Broadcasting
EBITDA						
1998 Pro Forma Broadcast Cash Flow	\$511.0	\$73.5	\$195.0	\$425.0	\$518.3	\$130.3
Less: Corp Overhead	(\$39.6)	(\$7.1)	(\$12.4)	(\$16.6)	(\$15.0)	(\$7.7)
1998 Pro Forma EBITDA	\$471.4	\$66.4	\$182.6	\$408.4	\$503.3	\$122.6
Senior Debt - Year-end 1998	\$1,539.0	\$13.0	\$500.0	\$1,579.8	\$809.6	\$45.6
Cash - Year-end 1998	(\$18.9)	(\$2.3)	(\$84.5)	(\$4.3)	(\$25.0)	(\$7.3)
Sub Debt/Unsecured Debt - Year-end 1998	\$0.0	\$401.8	\$2.5	\$950.9	\$0.0	\$570.0
Exchangeable Preferred - Year-end 1998	\$0.0	\$190.0	\$0.0	\$172.5	\$0.0	\$0.0
Leverage						
Senior Leverage	3.2	0.2	2.3	3.9	1.6	0.3
Senior and Sub Leverage	3.2	6.2	2.3	6.2	1.6	5.0
Total Leverage (Including Preferred)	3.2	9.1	2.3	6.6	1.6	5.0
Acquisition Capacity (Target Multiple of EBITDA)						
5.0	\$1,389.1	NA	\$823.5	NA	\$2,532.6	\$11.8
6.0	\$2,485.1	NA	\$1,291.5	NA	\$3,801.0	\$247.1
7.0	\$3,920.0	NA	\$1,902.3	\$413.5	\$5,454.2	\$557.5
Trading Multiples - Strength of Stock Currency						
Equity Market Capitalization	\$3,390.7	\$202.4	\$1,883.8	\$2,529.5	\$7,716.8	\$729.7
Debt/Pfd	\$1,520.1	\$602.5	\$418.0	\$2,698.9	\$784.6	\$608.3
Total Enterprise Value	\$4,910.8	\$804.9	\$2,301.8	\$5,228.4	\$8,501.4	\$1,338.0
1998 Pro Forma Broadcast Cash Flow	\$511.0	\$73.5	\$195.0	\$425.0	\$518.3	\$130.3
1998 Broadcast Cash Flow Multiple	9.4	11.0	11.8	12.3	11.2	10.3

Source: Bear, Stearns and Co. Inc. estimates.

- This chart is not a perfect representation of a company's acquisition capacity in one respect. Sinclair Broadcast Group has been able to readily acquire properties and raise cash through access to markets.

Opportunity Is Knocking: Positive Fundamental Trends in Broadcast TV

DYNAMIC DUO: 1999 AND 2000 COULD BE GOOD YEARS FOR ADVERTISING SPENDING

Although local television stations face a multitude of pressures (including declining audiences, increased competition, a more powerful radio industry, and slowing national advertising dollar growth), we expect these factors to be offset by a healthy advertising environment in 1999 and 2000 as corporations and marketers take advantage of the excitement created by the passage into the new millennium to promote their products and services.

Normally, advertising spending growth is anemic during odd-numbered years (as there are neither major political elections nor Olympic Games during these periods). But, as we see it, any enterprise that wants to promote itself as a 21st-century company, including automobile manufacturers, pharmaceutical companies, financial service providers, and technology-driven firms, should begin spending heavily now through 2000. At the forefront of this push will likely be the companies that have created the dominant 20th-century consumer brand-name franchises — such as Coca-Cola, McDonald's, Pepsi, and Wal-Mart.

In turn, we expect the broadcast television industry to be a major beneficiary of this strong advertising environment. In fact, we project that 2000 could be one of the best years for advertising in the history of the business. There is evidence to support our view. First, the Presidential election in 2000 has no incumbent, which is likely to require both parties to advertise more heavily than would otherwise be the case. Second, the overall growth in campaign advertising spending during Presidential election years continues to expand. Third, local television has been capturing a much bigger chunk of this political advertising spending in recent years. For example, in 1996, almost \$500 million was spent, with nearly 92% of these dollars flowing to the local television stations. This is in sharp contrast to the 1992 Presidential election year, when approximately \$300 million was spent on political advertising, and 75% of these dollars were channeled into the broadcast networks. Political spending surged by more than 175% at the local level in 1996, fueled by the overall increase in political advertising activity and the growing emphasis on local spending.

Exhibit 45. Estimated Annual Political Advertising Expenditures
(Gross dollars expended in millions of dollars)

Year	Type of Elections	Network	Stations	Total Political	Percent Network	Percent Stations
1980	Presidential	\$20,700	\$69,870	\$90,570	22.9%	77.1%
1981	Off Election Year	\$713	\$20,114	\$20,827	3.4%	96.6%
1982	Congressional	\$862	\$122,760	\$123,622	0.7%	99.3%
1983	Off Election Year	\$2,740	\$24,610	\$27,349	10.0%	90.0%
1984	Presidential	\$43,653	\$110,172	\$153,824	28.4%	71.6%
1985	Off Election Year	\$0	\$22,681	\$22,681	0.0%	100.0%
1986	Congressional	\$459	\$161,184	\$161,643	0.3%	99.7%
1987	Off Election Year	\$0	\$24,923	\$24,923	0.0%	100.0%
1988	Presidential	\$38,521	\$189,380	\$227,900	16.9%	83.1%
1989	Off Election Year	\$0	\$51,539	\$51,539	0.0%	100.0%
1990	Congressional	\$0	\$203,313	\$203,313	0.0%	100.0%
1991	Off Election Year	\$0	\$37,304	\$37,304	0.0%	100.0%
1992	Presidential	\$73,816	\$225,807	\$299,623	24.6%	75.4%
1993	Off Election Year	\$0	\$70,158	\$70,158	0.0%	100.0%
1994	Congressional	\$0	\$354,961	\$354,961	0.0%	100.0%
1995	Off Election Year	\$0	\$44,549	\$44,549	0.0%	100.0%
1996	Presidential	\$33,824	\$366,662	\$400,486	8.4%	91.6%
1997	Off Election Year	\$0	\$78,881	\$78,881	0.0%	100.0%

Congressional One-third of Senate, all of House, and about three-quarters of Governors

Off Election Year Some local and county elections

Source: Television Bureau of Advertising.

Historical evidence also supports our favorable outlook for TV advertising spending in 2000. Perhaps the best point of reference would be 1976, a year that featured the Summer Olympics in Montreal, a Presidential election, and the bicentennial celebrations. As Exhibit 46 illustrates, in 1976, television constant dollar advertising spending (to eliminate the effects of inflation) jumped nearly 21% in constant dollar terms — the industry's best performance during the past 35 years.

Exhibit 46. Total TV Advertising Growth in Constant Dollars

Year	Growth	Presidential	Congress	Summer Olympic	Winter Olympic	Other
1976	20.7%	Yes	Yes	Yes	Yes	U. S. Bicentennial; Carter vs. Ford
1984	14.4%	Yes	Yes	Yes	Yes	Mondale vs. Reagan
1972	11.1%	Yes	Yes	Yes	Yes	McGovern vs. Nixon
1964	11.0%	Yes	Yes	Yes	Yes	
1962	10.8%	No	Yes	No	No	
1983	10.0%	No	No	No	No	
1996	9.8%	Yes	Yes	Yes	No	Dole vs. Clinton
1978	9.7%	No	Yes	No	No	
1994	9.2%	No	Yes	No	Yes	
1966	9.1%	No	Yes	No	No	
1965	7.8%	No	No	No	No	
1982	7.4%	No	Yes	No	No	
1968	6.4%	Yes	Yes	Yes	Yes	Humphrey vs. Nixon
1977	6.4%	No	No	No	No	
1986	6.2%	No	Yes	No	No	
1969	6.0%	No	No	No	No	
1963	5.9%	No	No	No	No	
1992	5.1%	Yes	Yes	Yes	Yes	Clinton vs. Perot vs. Bush
1960	4.9%	Yes	Yes	Yes	Yes	Nixon vs. Kennedy
1979	4.5%	No	No	No	No	
1995	4.1%	No	No	No	No	
1988	3.9%	Yes	Yes	Yes	Yes	Dukakis vs. Bush
1980	3.6%	Yes	Yes	Yes	Yes	Reagan vs. Carter
1973	3.2%	No	No	No	No	
1997	2.9%	No	No	No	No	
1961	2.7%	No	No	No	No	
1985	2.7%	No	No	No	No	
1981	2.6%	No	No	No	No	
1990	1.5%	No	Yes	No	No	
1987	1.5%	No	No	No	No	
1993	1.4%	No	No	No	No	
1989	0.8%	No	No	No	No	
1974	-0.1%	No	Yes	No	No	
1967	-0.1%	No	No	No	No	
1975	-0.9%	No	No	No	No	
1970	-4.8%	No	Yes	No	No	
1971	-6.6%	No	No	No	No	Cigarette Advertising Banned
1991	-6.8%	No	No	No	No	Gulf War

Note: Growth rates have been adjusted on a 1992 constant dollar basis

Source: McCann Erickson Worldwide; Bear, Stearns & Co. Inc.

**DIGITAL DOLLARS:
MOVING FROM A CASH
DRAIN TO A VIABLE
BUSINESS AREA**

For broadcasters contemplating a move into the digital arena, the main challenge will be finding ways to transform a perceived cash flow drain into a thriving business. Although we believe there are several conceivable scenarios by which broadcasters with digital spectrum can create value, there are significant fundamental obstacles they will have to overcome. One positive is that the FCC has already written most of its rules governing digital broadcasting services, following nearly a decade of debate on standards, whether broadcasters would pay for their digital spectrum, channel assignments, power levels, and fee schedules.

Buildout and Return of Spectrum Is Expected

The first order of business addressed by the FCC was whether to grant broadcasters a second license for free or to make them pay for it. Ultimately, the FCC decided to grant the second license to broadcasters for development of digital services. In return, broadcasters are required to do two things. First, they must have digital services available by a specified time. Exhibit 47 summarizes the time requirements the FCC adopted in terms of the expected rollout of digital television. Second, broadcasters must return six MHz of spectrum in 2003, which will then be auctioned and turned over to a winner in 2006.

FCC Assigns Large Amount of Spectrum for Digital for Free

In March 1998, the FCC finalized a table of allocations designating the channel position of each digital channel granted to each existing television station. Part of this process concerned the amount of spectrum that would be allocated to digital. The FCC could have allocated channels 2 through 51 or channels 7 through 51 to the new "core spectrum." Obviously, broadcasters would prefer to have more rather than less spectrum. Ultimately, the FCC decided to allocate channels 2 through 51 to its core spectrum for digital television. We consider this a promising development, for several reasons.

- **Less Channel Interference.** The additional spectrum should minimize adjacent channel interference because channels can be allocated to broadcasters across a greater range of spectrum.
- **Fewer "Second Moves."** It will reduce the number of stations that will have to make a second move (i.e., if the broadcaster was allocated a station that was not in the core spectrum and later had to move when digital services became the only form of broadcast service after analog licenses were turned over for auction).
- **More Flexibility.** The additional spectrum should provide more flexibility for broadcasters to respond competitively as digital services are rolled out. Currently, interference, expected signal contours, and other aspects of the signal itself are merely theoretical constructs created by engineers.
- **A Sign of Support.** We believe that this move signals the FCC's commitment to the ultimate success of the new digital domain.

Exhibit 47. The Implementation of Digital Television

Planning Stage - Government

Assignment of Digital Licenses	Completed; Sixth Order/Rulemaking Issued in April 1997
Assignment of Power Allocations	Completed; Sixth Order/Rulemaking Issued in April 1997
Choose Core Spectrum for DTV	Completed; Provided More Spectrum (Channels 2-51 chosen over 7-51 or 2-46)
Use of DTV Spectrum	Completed; One channel must replicate analog programming; others can be free or pay services
Fees for Ancillary and Supplementary Services	Proposed Rulemaking Issued on December 19, 1997 - Basis is Percentage of Revenue of Incremental Profit
Permitting Broadcasters to Bid on Spectrum in 2003	Passed as Part of 1998 Budget Bill
Public Service Obligations	No Rulemaking; Presidential Advisory Committee Established on March 11, 1997; Recommendations October 1998
Review Process	Every Two Years

Technical/Operational Issues - Stations

Station Engineering Designs to Replicate Service Area	Ongoing; early stages for industry
Revamp Studios	Ongoing; early stages for industry
Choose DTV Format	Ongoing; early stages for industry; Minimal DTV standard is considered 1080-I or 720-P
Build/Lease New Towers	Ongoing; early stages for industry
Procure New Programming	Ongoing; early stages for industry
Challenges of Operating Two Stations Simultaneously	Ongoing; early stages for industry

Digital Television Timetable - Stations

ABC, CBS, NBC and Fox Affiliates in Top 10 Markets	May 1, 1999 (24 stations in top 10 markets committed to build facilities by November 1, 1998)
ABC, CBS, NBC and Fox Affiliates in Markets 11 Through 30	November 1, 1999
All Other Commercial Television Stations	May 1, 2002
All Other Non-Commercial Television Stations	May 1, 2003

Simulcast Requirements - Stations

Simulcast 50% of Analog Channel on Digital Channel	April 3, 2003
Simulcast 75% of Analog Channel on Digital Channel	April 3, 2004
Simulcast 100% of Analog Channel on Digital Channel	May 1, 2005

Implementation of Digital Television - Consumers

Purchase New Set-top Box	Options; Minimal Development
Purchase New Television Set	Options; Minimal Development
Purchase New Computer with DTV Capabilities	Options; Minimal Development

Implementation of Digital Television - Cable Broadcasters

Digital "Must Carry"	Congressional Hearings Week of April 20; FCC Proposed Rulemaking Expected 2Q 1998
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Source: Federal Communications Commission; Dow, Lohnes & Albertson; Covington & Burling; Bear, Stearns & Co. Inc.

FCC Powers Up UHF Stations

A few months ago, the FCC released a table of allocations that assigned a new digital channel to all operators of analog television channels. These included channel positions and guidelines on maximum power to be given to each operator of digital spectrum. The FCC believed that it was important to maintain the relative advantages enjoyed by VHF television stations over UHF stations in terms of reach (VHF signals travel farther than UHF signals). In order to achieve this, the FCC attempted to replicate a television station's Grade B signal contour (defined as satisfactory service expected at least 90% of the time for at least 50% of the receiving locations) to make it more similar to that of the operator's current analog signal. Since the vast majority of digital licenses will be UHF allocations, the FCC proposed maintaining the current VHF/UHF coverage disparity by increasing power allocations to those operators that operated VHF stations in a local market. However, by focusing on

replicating broadcaster's Grade B signal contours, power disparities would arise between operators of VHF and UHF spectrum. This is because, even though the current analog Grade A contours (defined as satisfactory service expected at least 90% of the time for at least 70% of the receiving locations) of a UHF and VHF station can be fairly similar in size, the Grade B contour of a VHF station reaches farther than that of a UHF station. So, by duplicating the Grade B contour, an existing VHF station, when granted higher power, is likely to extend its Grade A contour — to an extent that VHF stations may enjoy increased advantage over UHF stations (versus the analog signal).

In response to the allocation ruling, operators that owned a significant number of UHF properties, led by Sinclair Broadcast Group, petitioned the FCC to permit UHF stations to have increased power, provided the UHF station's Grade B contour did not extend beyond current service areas (by manipulation of the signal). These operators worried that power levels provided for UHF stations under the FCC's current allocations would have been insufficient to deliver video or ancillary services through buildings and other similar structures (while this would not be the case for VHF signals). We were also initially concerned that the degree of disparity in power levels between the VHF and UHF stations was too wide. In certain cases, local VHF stations were provided with power allocations that were up to 20 times greater than those of UHF stations. In our view, this would have had a significant impact on UHF operators' effectiveness in delivering emerging digital services.

On February 18, 1998, the FCC essentially answered the pleas of UHF operators by allowing them to enjoy the advantages of two technological changes now permitted, either one of which we believe can significantly improve the value of UHF stations' digital licenses relative to earlier proposals.

- **Increase Size of Service Area.** UHF stations (in fact, all television stations) will be permitted to increase their radiated power up to 200 kilowatts (if a station has been granted less than this) as long as the change in power will not result in more than a 2% increase in interference to the population served by another station in an adjacent market. (This is further qualified: if a station already experiences 10% interference to a population, and if raising the power to 200 kilowatts does not increase this interference to more than 10%, then it may do so.) This should expand a station's viable service area significantly.
- **Increase Power to Service Area.** UHF stations will be permitted to operate at one megawatt (1,000 kilowatts) within their service area. Previous proposals had provided power levels for UHF stations that approached 50 kilowatts. For these types of stations, the power level in the station's coverage area has been increased by nearly 20 times. In order to limit coverage of UHF stations relative to VHF stations (which, for the most part, were already granted one megawatt of power), UHF stations will be required to utilize "tilt-beam" technology to limit a UHF's station's signal coverage to its specified coverage area.

We believe that both of these proposals are big improvements over earlier plans. We could foresee a scenario whereby a UHF broadcaster could essentially take advantage of both these proposals simultaneously. For example, a UHF station could

increase its radiated power to 200 kilowatts in a market as long as it met the 2% adjacent market interference test. This would effectively establish the UHF station's coverage area. Then the UHF station could increase its power to one megawatt within this coverage area using tilt-beam technology. Ultimately, while UHF stations' signals may not reach as far over the horizon as a VHF station's (similar to today's reality), UHF stations should be very competitive (if not equal) to most VHF stations within the contour that denotes a typical UHF station's coverage area (i.e., usually the most densely populated area of a marketplace). We believe that power level increases will permit operators of UHF stations to compete more effectively with VHF stations in the digital world.

FCC Issues Proposed Fee Schedule for Ancillary Services

The first action taken by the FCC was to issue proposed fee schedules for ancillary services in digital television. This simply means that the government plans to take a "piece of the action" for revenues earned that are not related to the supply of free over-the-air television broadcasting. We consider this step another significant endorsement of ancillary services development.

Digital "Must Carry" Could Happen

As part of its upcoming rulemakings, the FCC will have to determine whether a broadcaster's digital signal should have "must carry" privileges similar to those of an analog signal. We believe that there is a decent chance that this will occur, for three reasons.

- We think Congress and the FCC would like to see some return for the digital licenses that were granted for free. This is precisely why we believe that one of the first issues the FCC tackled in digital television involved a fee schedule for ancillary services provided through the digital spectrum.
- We believe that the FCC would like to encourage the development of strong businesses models for the digital spectrum to ensure maximum values when the spectrum is eventually auctioned off. Recently, Congress suggested that future duopoly rules be relaxed to ultimately permit a broadcaster to bid on its own digital spectrum when auctions are held early in the next century. Creating viable bidders is always a good way to ensure an active bidding process at auction.
- Broadcasters are likely to argue that the industry has had to invest \$2-\$10 million per station to convert to digital (whether digital television [DTV] or high definition television [HDTV]), with no concomitant revenues associated with this investment, and that cable must bear some of the digital burden by helping to get new programming and services out to the subscriber base. The passage of digital must carry would be a clear victory for the broadcast television industry, in our view.

Important Hurdles in Digital TV

On February 18, 1998, broadcasters were officially provided with channel and power allocations. But before they can begin to launch these services, many hurdles must first be cleared.

- **Building or Retrofitting Towers.** One of the most vexing problems facing broadcasters will be finding tower capacity for the transmitters required to broadcast the digital signal. Many towers are unable to bear the weight of an additional transmitter, and therefore new towers must be built. This, in turn, poses further complications, such as dealing with local zoning and finding suppliers. We believe that there are only three major "tall tower" (broadcast tower) manufacturing companies currently in existence. Given the potentially huge demand for new towers and the dearth of tower builders, this step in the process may take longer than expected. In other cases, existing towers need to be retrofitted to strengthen them in order to absorb the weight of a new transmitter.
- **Slow Consumer Adoption.** Much of the success of digital television will likely depend on how quickly the consumer embraces these new services. We believe that several factors will slow the adoption of HDTV. First, sets have to be developed. Second, selling prices on the sets must reach "mass market" levels, which could take longer than anticipated, given the high initial cost of HDTV. If speculation is true, then early sets could cost as much as \$5,000-\$7,000 apiece. Many will argue that the prices of CD players, camcorders, and VCRs all were initially prohibitively expensive for the average consumer but nonetheless quickly become popular. However, we believe that there are three significant distinctions between these two product categories.

Existing Television Sets Work Well. CD players, VCRs, and camcorders were all breakthrough technologies that did not exist in any form prior to their development. By contrast, the average American household already has more than two television sets and, in our opinion, is not anxious to "write-off" television-set investments. This is why we believe the first wave of digital television may arrive through the average consumer's home in the form of a set-top box that will convert existing sets to digital technology. However, we believe that although the full potential of the HDTV could be quite spectacular, but we expect that set-top box conversions do not improve the picture significantly.

More Expensive. The proposed cost of early versions of digital television sets (\$5,000-\$7,000) would be five to seven times greater than that of the highest price paid for a VCR, camcorder, or CD player (which we estimate is between \$1,000 and \$1,500).

Longer Product Life Cycle. Based on our experience, we believe that the typical consumer will keep a television set for an average of ten to 15 years, while he or she would most likely replace a CD player, camcorder, or VCR much sooner. In general, we do not believe that the

average consumer will be willing to replace a television set that quickly, especially given the high cost of the new sets.

- **Digital Rollout Requires a Substantial Capital Outlay.** In order to build out digital television, we believe that television stations will need to spend \$2-\$8 million, depending on the depth of digital service provided. Pass-through of local signals should cost approximately \$2 million, while full-scale HDTV could cost \$8 million or more. This could be an expensive proposition for owners of 1) a significant number of properties (as digital spending could add up); 2) a significant number of small-market properties (as digital spending may be costly relative to the value of the property); and 3) large, dominant stations (which would be more likely to spend \$8-\$10 million on HDTV) — and with no guarantee of a significant payoff.
- **Initially, Broadcasters Benefit the Least.** We believe that broadcasters will be frustrated by the economics of digital television until its rollout becomes more broadly based. We believe that the broadcast business has the least to gain from the development of digital television, at least in the near term. While many industries have planned for several years to take advantage of digital television, as the development and manufacturing of new set-top boxes, television sets, computers and chip sets continues, television broadcasters did not know final power and channel allocations for their stations until the first quarter of 1998. Although they have the valuable asset (the spectrum), the broadcasters have had the least amount of time to develop the “real estate.”

Digital Television Has Potential; It's a Question of When

Despite significant issues facing the broadcast television industry as it contemplates an entry into digital television, we still believe that digital television holds promise. As we mentioned in the previous section, we think that to date, the broadcasters have had the least amount of time in which to develop economic models, as the final power and channel allocations were just recently granted. They have also lacked a clear vision for a broad rollout of these services. (Interestingly, I have been on four industry panels on digital television, featuring speakers from Time Warner Cable, HBO, Sarnoff Labs, DirectTV, and Microsoft, as well as representatives from the FCC and venture capitalists. Only one broadcaster has appeared — NBC.)

However, at first blush, we believe that several interesting economic models could develop, although the probability of success for these models remains unknown. As was mentioned in the introduction to this topic, the FCC and Congress did not specify how broadcasters must use their spectrum; a broadcaster merely has to supply digital television. If a broadcaster decides to pass along a signal that is not considered high definition, then it would have sufficient spectrum to undertake other services, such as time-shifted channel of core stations, new data services, or multicasting video.

Nonetheless, when broadcasters have publicized their intentions to multicast as part of their strategy to take advantage of this “spectrum flexibility,” they have been met with resounding criticism. While flexibility may be codified in law and at the FCC,

some members of Congress expect that the spectrum should be used for true high definition television for some portion of the day. We think it comes down to the degree in which each broadcaster provides the service. While some industry players believe that HDTV will be the best use of the new spectrum, others contend that a multicasting model will ultimately prove to be the most valuable use of the spectrum. In any respect, we doubt that local broadcasters will be able to make money until a large installed base of set-top boxes, television sets, or PCs has been established.

If broadcasters are unable to derive some interesting models on their own, we suspect there are enough other industries interested in the broadcaster's spectrum to create a supply/demand imbalance (there are more interested parties than spectrum available) Ultimately, we believe that broadcasters will have the opportunity to develop business models on their own or with partners.

Broadcasters Could Develop Their Own Models. In the long run, we believe that most broadcasters will air some number of hours of high definition television and that they should also be able to take advantage of spectrum flexibility during those hours in which a broadcaster chooses to take advantage of compression in a "low definition" environment. We surmise that many operators will explore models that take advantage of the ability to compress the digital signal, including datacasting, multicasting, and creating a competitive cable service.

- **Datacasting.** Datacasting is over-the-air transmission of data (text, voice, or video) such as stock quotes, publications (e.g., newspaper contents), Web sites, etc. Two companies have explored the potential of datacasting using the sideband or vertical interval of the conventional ATSC signal to broadcast data to receivers, such as personal computers: Sinclair Broadcast Group and Datacast, a joint effort by LIN Television, Chris-Craft, Granite Broadcasting, and Shurz Communications. We have seen both of these technologies and consider them promising. One of the more interesting potential applications allows data to be downloaded from the Web onto a computer without any delays caused by busy servers, constrained phone lines, or slow modems. Ultimately, we believe that the full potential of the digital spectrum will be tapped when the viability (if there is a viable business) of digital broadcasting comes to the attention of a technology company that decides to make a sizable investment in its development.
- **Multicasting.** Multicasting involves the compression of a broadcast television signal into multiple video channels that could be used to 1) time-shift existing programming schedules to permit viewers to watch a show at different times of the day; 2) create a 24-hour-a-day local news channel; 3) lease to other programmers that cannot clear their shows in a marketplace; 4) lease to a cable network that may not be carried on local cable systems; or 5) create a competitive multichannel video service versus cable by combining the digital signals of a few local broadcasters in a local market.
- **Competitive Multichannel Entry.** We are also intrigued by the broadcast television industry's potential for creating an alternative multichannel service to cable. In prime time, the six networks combined deliver nearly 70% of all the

viewing audience in television, but the local stations generally do not earn any subscriber fees whatsoever. And the potential subscription pie for television broadcasters is large. We estimate that there are 65 million cable households in the United States. On average, the local cable system charges approximately \$10 per month for "lifeline" service, which entitles a subscriber access to all of the over-the-air broadcast television stations only. This translates into revenues of an estimated \$650 million per month, or \$7.8 billion per year, for the cable multiple system operators (MSOs). In our view, the programming expense associated with these revenues is not meaningful, implying that the lifeline service generates billions of dollars in cash flow for the cable industry. In fact, cable operators may make more money on "free" over-the-air broadcasts than the broadcast industry does. Moreover, while the FCC and Congress appear reluctant to pass legislation or adapt rulemakings that would apply pressure on cable companies to change rates, we believe that they are both very interested in encouraging the development of viable competitors to cable.

One unique way that broadcasters could possibly get paid for their broadcast signals would be to create multicasting joint ventures to sell multichannel services. Under this approach, a group of broadcasters would contribute their digital spectrum, compress the spectrum, and offer it to cable networks and local broadcast affiliates — essentially creating an over-the-air MSO.

The ability of television broadcasters to participate in this revenue stream would be a significant positive for the industry, in our opinion. However, from our initial discussions with broadcasters, Washington sources, and industry players, this model could encounter big obstacles, including 1) getting local broadcasters, which are used to competing, to cooperate with each other; 2) figuring out how to access programming competitively (there is a new bill in Congress [H.R. 2555] that would provide broadcasters equal access of cable programming at equal cost, but the prospects for the bill do not look good); 3) finding ways to share the economics; 4) making sure sufficient digital signals (towers and transmitters) are built; and 5) developing a digital set-top box. While we doubt that these impediments can be overcome in the near term, we find this idea very compelling.

Broadcasters Could Develop Models with Other Constituents. Although broadcasters could create business models on their own, we still believe that other promising concepts could develop between broadcasters and other parties seeking a presence in digital television. In our view, as long as there is more demand for the digital spectrum from industries interested in exploiting and developing it (e.g., consumer electronics companies, computer manufacturers, set-top box manufacturers, direct broadcast satellite providers, cable multiple system operators, venture capitalists, and chip manufacturers) than spectrum available, opportunities for digital television (and for the broadcasters) will open up. We highlight two possible partners with which TV broadcasters could join to play the digital television potential — cable operators and direct broadcast satellite providers.

- **Cable Systems and Television Broadcasters: Perfect Together?** We believe that the advent of digital television may offer an unprecedented opportunity for

local broadcasters and cable systems to cooperate. The confluence of a few events in the context of the digital world could make this happen: 1) we believe that it is essential for local broadcasters to participate in the economics of subscription fees; 2) cable systems are rapidly expanding channel capacity and need programming for these channels; and 3) direct broadcast satellite (DBS) systems are appealing to Congress and the FCC to permit them to rebroadcast television signals within local markets.

In light of these three facts, we believe that cable systems could establish a digital broadcast tier that could be programmed by local broadcasters, which could, in turn, be paid a subscription fee. This model could work because it can fulfill many of the goals of a number of key constituents. It would create a supply of programming for cable MSOs in the process of or seeking to expand channel capacity. It would help cable systems save face by not having to pay retransmission consent rights. Such a development would also allow broadcasters to participate in subscription fees and turn up the competitive heat on DBS operators to provide all local signals, not just the primary signal. In fact, we believe it probably behooves the cable industry to actually seek out digital must carry rules, which could spur DBS companies to do the same. As DBS providers are currently unable to carry all existing analog signals, it would be more difficult to carry two local signals for each station.

- **DBS and Television Broadcasters: An Advertising Opportunity.** We suspect that DBS providers may also have a distinct interest in creating a relationship with the local broadcaster and that they can provide something that cable cannot — that is, the ability to sell local cable network advertising inventory on behalf of the DBS providers. In the broadcast world of the not-too-distant future, a significant number of broadcasters will be airing a digital signal. DBS providers would ultimately like to create antennae technology that could receive the broadcasters' digital signals and weave these signals into the DBS programming universe as seamlessly as possible. Having a strong penetration within the DBS universe is attractive for many reasons.

Another Platform. It makes broadcast television's signal resident on another distribution platform.

Logical Partners. We believe it would be logical for DBS operators to enter into relationships with local broadcasters, as such a move would permit the broadcasters to sell local ad inventory on behalf of the national DBS companies, which lack the salesforce infrastructure to sell local ad time. This could be significant for two reasons: 1) it could provide another opportunity for broadcasters to sell ad time, and 2) local cable systems are becoming more competitive with local television stations in vying for local advertising. To the degree that DBS penetration affects local cable penetration, the broadcaster may benefit.

Capturing the Value of Retransmission Consent. In the medium- to long-term time frame, if DBS penetration ever reaches critical mass, it may provide a competitive environment between cable and DBS that

could permit TV broadcasters to capture the theoretical value that retransmission consent could represent.

We believe that DBS' current impact on the television business is minimal. DBS penetration rates remain low, and legislation permitting local broadcast signals to be retransmitted by DBS companies into local markets must be written. While we believe that DBS operators will be able to address the local signal issue over time, the local signal problem for DBS may be exacerbated, in our view, by the advent of digital television. The challenge to this industry will then be in finding ways to carry both a primary analog television signal and a local station's digital signal, at a time when it is difficult to carry just one local signal.

High Definition Television as a Model. Many broadcasters are mulling over a possible entry into high definition television. We think there are a couple of ways that such a move could prove fruitful. First, it could be argued that the superior visual image provided by HDTV may draw more viewers back to local television stations. Since advertising rates are set on a cost per thousand basis, incremental viewership would translate into incremental rate increases for the advertiser (and additional revenues for the broadcaster). Or broadcasters may decide to deploy HDTV and charge higher rates for what may be perceived as an exceptional programming environment.

Although the potential impact of HDTV on viewership, as well as the willingness of advertisers to pay higher advertising rates, is unknown at this time, we think this idea is worth exploring. The look of high definition television is truly superior to today's video offerings, especially for special programming such as movies or sporting events. We could make a case that marketers would be willing to pay more money to advertise on the programs that are broadcast to take advantage of HDTV's higher-quality visual domain. Moreover, since it is very unlikely that every local station will deploy HDTV, the amount of advertising inventory that can be sold within an HDTV environment should be limited. Also, there are plenty of examples whereby advertisers have proved willing to pay more money to advertise their products or services in a more distinctive environment or novel way, including:

- color advertising in newspapers versus black-and-white advertisements;
- color advertising in magazines versus black-and-white advertisements;
- running ads during a television program rather than during the transition between two programs (called adjacents); and
- running ads in the Sunday morning magazines rather than in the body of the newspaper itself.

Will Broadcasters Ever Force the Retransmission Consent Issue?

Another way that local TV broadcasters could possibly receive compensation from local cable operators would be to urge the major broadcast networks to ask for cash payments for retransmission of local broadcast signals in the next round of

retransmission elections, which we believe will take place in 1999. The broadcast networks have abstained from pressing the retransmission issue, even though one of their own, CBS, had originally led the charge to secure retransmission consent as a reality. We believe that the broadcast networks have essentially used their retransmission consent negotiations to secure carriage of their own cable networks, such as MSNBC, fX, Fox News, and CBS's Eye on People. However, as we believe that we've reached the theoretical maximum number of mass-market cable networks, we don't think it will be in the broadcast networks' best interest to launch more cable networks. Recent retransmission launches, such as CBS Eye on People, still have very weak distribution. In addition, for the most part, the networks have substantially increased their base of owned and operated television properties, which all could benefit from retransmission consent payments. Lastly, at the network level, the economics are being weakened from the increased competition for high-profile programming such as "NFL Football" and "ER." Retransmission consent may be an alternative to improve this situation.

Nonetheless, the broadcast networks may not choose to act quickly on the retransmission promise, mainly because 1) they may not want to risk the decrease in ratings and advertising revenues that could accompany not being carried by cable (if cable operators indeed decide not to pay subscriber fees) and 2) they may not want to risk being the only, or one of the only, networks that "draws a line in the sand." These issues notwithstanding, we continue to believe that the broadcast television industry must search for ways to tap the subscription fee business.

DISCREPANCIES IN VALUATIONS ARE TOO WIDE

The disparity in private versus public valuations between the broadcast television stocks and the radio stocks appears to be wider than ever. In Exhibit 48, we provide a summary of some of the larger recent private market transactions that have occurred in the radio and broadcast television industries. In general, radio has sold at a multiple of 15x-19x 12-month trailing broadcast cash flow, while television broadcasters have fetched 12.5x-14.0x trailing BCF.

Exhibit 48. Recent TV and Radio Broadcasting M&A Transactions

Date Announced	Acquiror	Target	Total Purchase Price	Current Year BCF	Current Year Multiple
Television					
Mar-98	Emmis Broadcasting	SF Broadcasting	\$307.0	\$14.0	21.9
Feb-98	Sinclair Broadcast Group	Sullivan Broadcasting	1000.0	82.0	12.2
Dec-97	Sinclair Broadcast Group	Max Media	255.0	18.0	14.2
Aug-97	Hicks, Muse, Tate & Furst	LIN Television	1949.2 ⁽¹⁾	145.5	13.4
Jul-97	Sinclair Broadcast Group	Heritage Broadcasting	630.0	43.4	14.5
Mar-97	Argyle Television	Hearst Corporation	539.5	41.5	13.0
Jan-97	First Media	Meredith Corporation	435	32.1	13.6
Jul-96	Tribune Co.	Renaissance	1150.8	84.4	13.6
Radio					
Oct-97	Jacor	Nationwide Mutual Insurance	420.0	27.0	15.6
Sep-97	Westinghouse/CBS	American Radio Systems	2600.0	137.0	19.0
Aug-97	Hicks Muse/Capstar	SFX Broadcasting	1954.4	130.0	15.0
Jun-97	Clear Channel	Paxson Communications Radio and Outdoor	663.0	30	22.1

Includes Dallas but excludes Grand Rapids.

Source: Bear, Stearns and Co. Inc. estimates.

However, while radio stocks are trading at an average 13.0x-16.0x forward BCF, at or close to private market value, the broadcast television stocks are selling at 9.0x-

12.0x forward cash flow, implying a steeper disparity to private market values relative to the radio equities. Given the rapid industry consolidation, we believe that the trading multiples of the major consolidators and the broadcasters that sell into the aggressive acquisition bidding environment should experience the most multiple expansion.

Exhibit 49. Comp Sheet

		A.H. Belo Corporation	Granite Broadcasting	Hearst Argyle Television	Sinclair Broadcast Group	USA Networks	Young Broadcasting
Ticker		BLC	GBTVK	HATV	SBGI	USAI	YBTVA
Shares	Fully Diluted Shares Outstanding (Treasury Method)	63.9	18.4	54.8	48.4	339.2	15.0
	Float (May 21, 1998)	50.2	9.0	10.4	24.0	74.4	12.0
	Float - \$	\$2,663.7	\$99.0	\$357.5	\$1,254.0	\$1,692.6	\$582.0
Current Price - May 21, 1998		\$53.06	\$11.00	\$34.38	\$52.25	\$22.75	\$48.50
Capitalization	Equity - At Market	\$3,390.7	\$202.4	\$1,883.7	\$2,529.5	\$7,716.8	\$729.7
	Preferred Stock-Exchangeable	\$0.0	\$190.0	\$0.0	\$172.5	\$0.0	\$0.0
	High Yield Trust Offered Preferred Securities	\$0.0	\$0.0	\$0.0	\$200.0	\$0.0	\$0.0
	Year-End Net Debt - 1998	\$1,520.1	\$412.5	\$418.0	\$2,326.4	\$784.6	\$608.3
	Capitalization	\$4,910.8	\$804.9	\$2,301.7	\$5,228.4	\$8,501.4	\$1,338.0
Free Cash Flow (FCF)	1998E	\$112.0	\$8.6	\$80.8	\$10.5	(\$14.5)	\$46.2
	1999E	\$152.6	(\$2.8)	\$90.3	\$128.0	\$87.9	\$59.6
FCF Per Share	1998E	\$1.77	\$0.47	\$1.50	\$0.23	(\$0.04)	\$3.27
	1999E	\$2.41	(\$0.15)	\$1.68	\$2.68	\$0.26	\$4.23
Growth in FCF per Share	1998E	-28.0%	193.8%	NA	-87.2%	NA	43.4%
	1999E	36.2%	-131.9%	12.0%	1065.2%	NA	29.4%
FCF Multiple	1998E	30.0x	23.4x	22.9x	227.2x	NA	14.8x
	1999E	22.0x	(73.3x)	20.5x	19.5x	NA	11.5x
Broadcast Cash Flow (BCF) (\$ Millions)	1997 - Pro Forma	\$450.8	\$67.2	\$175.7	\$401.0	\$460.8	\$118.2
	1997 - Reported	\$413.9	\$69.8	\$92.7	\$243.4	\$199.5	\$118.2
	1998E - Pro Forma	\$511.0	\$73.5	\$195.0	\$425.0	\$518.3	\$130.3
	1998E - Reported	\$511.0	\$76.2	\$194.6	\$356.8	NA	\$130.3
	1999E	\$549.3	\$82.2	\$215.8	\$456.2	\$623.6	\$138.7
Growth in BCF	1998E - Pro Forma	13.4%	9.4%	11.0%	6.0%	12.5%	10.2%
	1999E	7.5%	11.8%	10.7%	7.3%	20.3%	6.4%
BCF Multiples	1997 - Pro Forma	10.6x	12.0x	13.1x	13.0x	NA	11.3x
	1998E - Pro Forma	9.4x	11.0x	11.8x	12.3x	11.2x	10.3x
	1999E	8.7x	9.8x	10.7x	11.5x	9.3x	9.6x

Source: Bear, Stearns and Co. Inc. estimates.

DO OR DIE TIME

Will the Television Acquisition Scene Become Hostile?

In the past, the M&A market for broadcast television would be characterized as civilized. Hostile or unwanted solicitations have long been anathema to the industry, and most properties were sold through auctions or private transactions. However, we're seeing signs that the acquisition climate could grow much harsher over the next few years.

- **A Long List of Suitors . . .** There is a growing number of television operators (including Hearst-Argyle Television, Sinclair Broadcast Group, A.H. Belo Corp.,

LIN Television/Chancellor Broadcasting, and the Retirement Fund of Alabama (Raycom) that have stated their intentions to attain market share of 20% or more of television households. Given the caliber (and financial health) of this group of consolidators, there will likely be tremendous pressure to find and purchase broadcast properties.

- **... And a Dearth of Available Properties.** The number of television properties for sale, including individual stations and groups, has shrunk considerably, as literally dozens and dozens of operators have exited the business during the first wave of consolidation during the past five years.

Exhibit 50. Names of Operators That Have Left the Business

1 Adams Communications	13 Phipps-Potamkin	25 Superior Broadcasting	37 Koplar Communications
2 Busse Broadcasting	14 SJL Broadcasting	26 Brissette Broadcasting	38 Cottonwood Communications
3 Boston Celtics, LP	15 Narragansett	27 Renaissance Communications	39 Max Media
4 Cannon/McKinnon	16 Queen City	28 New World Communications	40 Busse Broadcasting
5 Continental Broadcasting	17 Act III Broadcasting	29 SF Broadcasting	41 Decatur Foursquare Broadcasting
6 Cook Inlet	18 Outlet Communications	30 AFLAC	42 Dudley Communications
7 Gillett Holdings	19 Multimedia, Inc.	31 Federal Broadcasting	43 Cooper Family
8 Heritage Media	20 Beasley Broadcasting	32 Pezold Broadcasting	44 River City Broadcasting
9 Krypton Broadcasting	21 River City Broadcasting	33 Providence Journal	45 Malrite Communications
10 Nationwide Communications	22 Palmer Communications	34 Harte-Hanks Communications	46 Blackstar
11 New Vision Communications	23 Ellis Communications	35 LIN Television Corp.	47 Pulitzer (expected)
12 Northstar Television Group	24 ABRY Holdings	36 LIN Broadcasting Corp.	48 Guy Gannett (expected)

Source: *Broadcasting & Cable*; company releases.

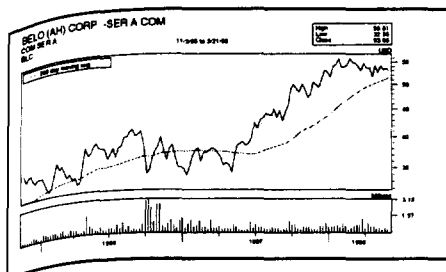
- **Competitive Realities Favor Larger Players.** As the industry consolidates and as competitive threats continue to mount, we believe that broadcasters are increasingly recognizing the importance of building large distribution platforms.
- **New Tax Laws Could Encourage Selling.** Recent changes in the capital gains tax laws should theoretically encourage the sale of television properties owned by individuals, although few properties have come to market so far.
- **It's a Seller's Market.** We believe that the fundamental demand/supply equation for the acquisition of television broadcasting properties has never been so out of sync and that this factor should also convince sellers that this is a good time to make a move.

We believe the combination of the aforementioned factors could create a more antagonistic bidding environment for broadcast properties, which may trigger 1) fiercely competitive bidding wars among the various groups (such as the battle for Pulitzer's broadcast properties); 2) unsolicited bids to purchase public companies; and 3) more proactive bidding for private companies.

One recent sign that things are starting to change came from Raycom (controlled by the Retirement Fund of Alabama), which placed a higher bid on LIN Television's assets after Hicks, Muse and NBC (General Electric) had already "won" a long auction process. Although Raycom did not ultimately prevail, the unexpected bid created incremental value for LIN Television Corp.'s public shareholders. Given the industry's push for scale and the dwindling list of available properties, bidding wars should bring higher prices for broadcast TV assets.

Company Profiles

A.H. BELO CORP. (BLC-53¹/₁₆)



52-Week Range
\$57-\$38

EPS
12/97: \$1.41
12/98E: \$1.69
12/99E: \$2.18

P/E
12/98E: 31.4x
12/99E: 24.3x

BCF (mil)
12/97PF: \$450.8
12/98PFE: \$511.0
12/99PFE: \$549.3

EV/EBITDA
12/98PFE: 9.4x
12/99PFE: 8.7x

Dividend
\$0.48

Yield
0.9%

Com. Shares (mil)
63.9

Equity Market Capitalization (mil)
\$3,391

Debt/EBITDA (1998E)
3.2x

Est. 3-Yr BCF Growth Rate
10.5%

Balance, Size, Quality Assets, and Decisive Management

We remain very bullish on BLC shares, as we believe the company's diversified portfolio of newspaper and broadcast assets and the quality of these properties (the broadcast operations enjoy some of the highest audiences and syndicator reaches of the companies we follow) should pave the way for above-average BCF growth over the next few years. We are impressed with the caliber of the company's management, which has clearly articulated its goals and has acted decisively to attain them. Broadcast cash flow could climb 13.4% in 1998, followed by a 7.5% pickup in 1999. Despite these prospects, the stock sells at one of the lowest BCF multiples in the group based on our 1998 and 1999 estimates. We attribute this disparity to the stock's general lack of visibility within the investment community, as well as to the company's newspaper assets, which tend to command lower valuations relative to television.

- **Quality of Assets Justifies Premium Valuation.** Based on an enterprise value of \$4.9 billion (incorporating 63.9 million fully diluted shares, using the treasury method, and projected year-end debt of \$1.5 billion), we estimate that BLC shares are trading at a blended multiple of 9.5x for the TV properties and the newspaper assets. In our view, the company's hidden assets, which include the value of the LMAs, Belo Production (which owns "Beakman's World," a show in syndication), stock in Peapod, NorthWest Cable News, and a 7% stake in Falcon Cable, LP, approach approximately \$118 million (nearly \$2 per share). If we assign the television properties a multiple of 11.0x 1999 operating cash flow and the newspaper assets a multiple of 9.5x 1999 OCF, and then add in the value of the hidden assets, we arrive at a year-end 1999 target price of \$69 for the stock. We believe that these target multiples more appropriately reflect the company's excellent investment merits and its above-average growth prospects.

- **Successful Reorientation of Asset Mix.** In 1996, Belo launched a major overhaul of its asset mix in order to place more emphasis on television. After several acquisitions and asset swaps, the company's properties now reach 14.2% of all U.S. television households, ranking it as the third-largest non-network-affiliated television group in the country. Belo's average TV rating (TV households tuned to its stations as a percentage of total TV households) is the second highest in the country, placing it behind the owned and operated TV stations run by ABC. Because of this makeover, television assets are expected to contribute an estimated 53.6% of total BCF in 1998

versus 49% in 1996 (we note that the company's impressive progress on the television side has been somewhat masked by the phenomenal cash flow growth of *The Dallas Morning News*, a prominent and highly profitable newspaper).

- **Diversity in Network Affiliation.** We believe that Belo has achieved the best balance among the various Big Three network affiliations of the companies we follow. The importance of this factor was accentuated by the recent negotiations for the NFL Football rights. Belo is the second-largest CBS affiliate group (4.9% of TV households), the third-largest NBC affiliate group (4.0%), and the fifth-largest ABC affiliate group (4.3%). We like to see this level of affiliation balance, as it helps to buffer the broadcaster against the negative impact caused by shifts in high-profile programming.
- **Dual-Media Presence in a Number of Local Markets.** The company has also met with good success in developing second television "voices" in a number of its local markets by forming local marketing agreements (in which one owner of a station pays another owner a fee for the right to program and sell the advertising time of another station in the market) and local cable news networks. For example, as part of the recent acquisition of The Providence Journal Company, Belo assumed control of operations of four LMAs, located in Seattle, Tucson, Boise, and Honolulu. The company also acquired NorthWest Cable News, a regional cable news network that repackages the local news product of the four network-affiliated television stations in Seattle, Portland, Spokane, and Boise and sells advertising, thereby expanding its revenue sources from news programming. Belo plans to replicate this concept by launching Texas Cable News (possibly in the third quarter), a regional cable news channel that will access the programming from the company's Dallas, Houston, and San Antonio stations. The company also operates *The Dallas Morning News*, the sole metro paper in that market.
- **Emphasis on Gross Cash Flow Earned, Not Margin.** Belo has emphasized the generation of the greatest level of absolute cash flow in a particular market as opposed to delivering the highest cash flow margins. In our view, this emphasis is an outgrowth of Belo's commitment to building strong local franchises, which require 1) higher-quality (and often more expensive) purchased television programming; 2) higher-quality (and often more expensive) television news programming; and 3) a strong commitment to journalistic excellence, which can require additional manpower. However, as we see it, Belo's operating results are the strongest testament to the wisdom of this strategic thinking.
- **Improving Results at Former Providence Journal Properties.** Belo has done an excellent job of integrating the Providence Journal assets. In television, the company has seized upon the strong ratings

and franchise to build momentum and push margins higher. Specifically, margins at the broadcast division are expected to expand to 42.2% in 1998 from 36.8% in 1996. In newspapers, Belo is benefiting from the turnaround in the Providence market as well as the recent restructuring of the newspaper division. Both Factors are driving top-line and operating cash flow growth. While management has not placed as much focus on newspaper acquisitions relative to television acquisitions, we still expect it to add to this portfolio as attractive opportunities arise.

- **Planning a Move into HDTV.** Belo's commitment to the development of high definition television has been unwavering. If anything, the company has become even more emboldened by the enthusiasm shown by consumers who came to view the new technology at the Texas State Fair last summer. It has already converted its station in Dallas to HDTV and expects to launch the new technology at its stations in Houston and Seattle shortly.
- **Maintaining a Conservative Capital Structure.** Belo's management has always maintained conservative levels of debt. By year-end 1998, we expect that the company should have approximately \$1.5 billion of debt and \$471.4 million in EBITDA, which represents leverage of 3.2x — this is very conservative, especially relative to the capital structures of comparable companies. This leverage should permit the company to take advantage of other transactional opportunities.

FULFILLING ITS STRATEGIC GOALS

Build a Larger Television Station Group

In 1996, A.H. Belo made a strategic decision to reorient the mix of its asset base to emphasize television. In September of that year, the company announced its intention to acquire The Providence Journal Company for \$1.5 billion and added nine television stations (NBC affiliates in Seattle, Portland, Charlotte, Honolulu, and Boise; an ABC affiliate in Louisville; Fox affiliates in Albuquerque and Tucson; and a CBS affiliate in Spokane). After the Providence Journal acquisition, the company owned two stations in the Seattle market: KING-TV, the NBC affiliate, and KIRO-TV, which at the time was an independent. Belo successfully entered into a three-way swap between Cox Enterprises and Viacom, which added KMOV-TV, the CBS affiliate in St. Louis to the company's portfolio.

The most recent acquisition occurred through another creative swap of assets. In the Providence Journal acquisition, Belo acquired the TV Food Network, a basic cable network. It swapped this asset and \$75 million with Scripps-Howard for KENS-TV in San Antonio. Belo now owns a television property in the largest three Texas markets.

As a result of all this acquisition and swap activity, Belo has amassed considerable leverage in the television business, and its properties now reach 14.2% of all U.S. television households, making it the third-largest non-network-affiliated television

station group in the country. In addition, the reorientation of Belo's asset base has changed the mix of cash flow contribution of the television division. In 1998, we expect that the television properties should deliver approximately 53.6% of the company's cash flow, up from about 49% in 1996. In our view, the phenomenal cash growth of *The Dallas Morning News* disguises the actual change in asset mix within the company.

Creating Second Television Voices in Local Markets

Belo has also had great success in creating second television voices in several of its local markets. With the Providence Journal acquisition, the company inherited two of these second voices, namely local cable channels and local marketing agreements. As mentioned above, The company purchased television stations in Seattle, Portland, Boise, and Spokane from Providence Journal. Before these properties were acquired, Providence Journal had launched a regional cable network called NorthWest Cable News, which now shares news coverage generated at Belo's regional affiliates and provides a second video outlet in these four fast-growing markets. The cable network, which we estimate reaches 1.4 million television households, is doing well and is approaching breakeven.

Also as part of the purchase of The Providence Journal Company, Belo inherited LMAs in four television markets — Seattle, Honolulu, Tucson, and Boise. In these four markets, the LMAs permit the company to program and sell advertising inventory on two properties. In two cases, Seattle and Boise, Belo has the option to purchase the stations should duopoly rules change. In Seattle, its second-largest television market, Belo has three video outlets; the owned and operated television station (KING-TV), the station operated under an LMA (KONG-TV), and the cable network (NorthWest Cable News). In Dallas, the company is expected to soon launch a cable network, Texas Cable News, which we believe should reach 1.2 million cable subscribers.

Building Substantial Local Franchises

At the heart of Belo's growth strategy is its emphasis on building strong local franchises, which management believes goes hand in hand with securing their stations' position as important advertising vehicles for local and national advertisers. The company's success in achieving this goal is the biggest reason why we think the assets deserve a premium valuation. Belo develops properties that are popular with local viewers and readers and enjoy strong community awareness and therefore become an integral part of an advertiser's local "buy." For example, *The Dallas Morning News* has more advertising lineage than any other newspaper in the United States. Also, Belo's average rating (TV households tuned to Belo's stations as a percentage of total TV households) is the second highest in the U.S., ranking only behind the owned and operated television stations run by ABC. The company also holds the No. 1 or No. 2 television station in nine of its 13 markets, which suggests that it should garner a disproportionate amount of political advertising dollars during election years. Through these strong local television franchises, the company should enjoy substantial leverage with advertisers (which benefit from the station's strong recognition within the local community), programmers (which want the strongest

distribution platform for programs), and networks (which benefit by selling national advertising and winning network ratings races).

Maintain Good Affiliation Balance at Television Properties

We believe that Belo has attained the best balance in its various affiliations (ABC, CBS, and NBC) of any broadcaster we follow. As we discussed in the overview of the industry, maintaining a good affiliation balance has become increasingly important as the broadcast networks grow more powerful.

The significance of this point took on special relevance with the turn of events surrounding renegotiations of the NFL Football rights this past year. Belo is the second-largest CBS affiliate group (4.9% of TV households), the third-largest NBC affiliate group (4.0%), and the fifth-largest ABC affiliate group (4.3%) in the country. With the American Football Conference moving to CBS, the company's NBC stations could get hurt, especially in Seattle, but CBS affiliates will benefit. Belo should also benefit from ABC's renewal of Monday Night Football because the games will begin at 8:00 p.m. in 1998 instead of 9:00 p.m. as they have in the past. In many of its markets, this will permit Belo to run its late news about 45 minutes earlier, when audience are larger and more ad dollars can be earned. The number of viewers watching television from 8:00 p.m. to 9:00 p.m. is certainly higher than those watching from 11:00 p.m. to 12:00 a.m., which should benefit the company's late news flow and profitability on its ABC affiliates. Although Belo is not committed to sharing some of the burden of increased rights fees paid by the networks during negotiations for football, it has stated that it would maintain "an open mind." We will continue to monitor the extent to which the company actually bears any burden.

Adding to Its Publishing Portfolio as Opportunities Arise

Belo has been paying equivalent attention to building its portfolio of newspaper assets, and we believe that its current properties should continue to perform well and that the broadcaster will add to its newspaper holdings if attractive opportunities arise. The company's recent purchase of the remaining stake in *The Press-Enterprise* in Riverside, California, exemplifies this strategic thinking. We believe that Belo will place its stamp on this newspaper, in which it recently increased its stake to 100% from roughly 38% on July 25, 1997, for an amount we estimate at close to \$125 million. By our estimates, this property generates roughly \$15-\$17 million in cash flow. Overall, we think that the company purchased this newspaper for a blended multiple that approaches 10.0x, which we consider extremely reasonable given the property's upside potential under Belo's guidance and the anticipated growth in this market (after a long slump).

Improving Results at Former Providence Journal Properties

We believe that Belo has done an extremely good job in melding the Providence Journal assets into the corporate fold and bringing these operations up to speed. In television, the company is seizing upon strong ratings, franchise-building momentum, and recent successful management changes to push margins higher.

Margins rose to 36.8% at the broadcast division in 1996 and are expected to expand to 42.2% in 1998. In newspapers, Belo is benefiting from the turnaround in the Providence market as well as from the recent restructuring of the newspaper division, both of which are driving top-line and operating cash flow growth.

Shedding Nonstrategic or Non-Cash-Flow-Producing Assets

At the time it acquired Providence Journal, Belo vowed to sell, close down, or swap assets that were not of strategic value or that were cash flow drains. At America's Health Network (AHN) basic cable channel, the company refused to fund additional losses, made an attempt to earn a potential financial return on the company's 65% ownership interest (with Columbia/HCA), and eventually turned the keys over to the existing partners in order to achieve its primary goal — that is, to not fund AHN's losses. In August, Belo agreed to swap its 45% interest in the Television Food Network (TVFN) and \$75 million for KENS-TV with Scripps-Howard, accomplishing two goals. First, it avoided having to fund incremental losses at TVFN and, second, it increased its presence in the television business. We believe that the transaction should bolster free cash flow to the tune of \$26 million in 1998.

Committing to High Definition Television

Belo has an unwavering commitment to the development of high definition television. If anything, the company has become even more emboldened by the enthusiasm shown by consumers who came to view the new technology at the Texas State Fair last summer. It has already converted its station in Dallas to HDTV and expects to launch the new technology at its stations in Houston and Seattle soon.

In the case of HDTV, we think there are two plausible ways for broadcasters to create value. First, it could also be argued that the superior visual image of HDTV will draw more viewers back to local television stations. Since advertising rates are set on a cost per thousand basis, incremental viewership should translate into incremental rates and revenues. Second, broadcasters could deploy HDTV and seek higher rates for what may be perceived as a superior programming environment. Although it is still unknown how consumers will greet HDTV and whether advertisers will be willing to pay higher advertising rates, we find the concept intriguing. The look of HDTV is truly better than today's video offerings, especially for delivering special programming such as movies or sporting events. We can make a case that marketers may be willing to pay more money to advertise in those programs that are broadcast to take advantage of HDTV's higher-quality visual domain. Also, it is very unlikely that every local station will deploy HDTV, which should limit the amount of advertising inventory that can be sold within an HDTV environment. This kind of differentiation already occurs in the media business to some extent. For example, advertising rates for color ads are higher than those for black and white because the color ad is more sophisticated.

FIRST-QUARTER 1998 SNAPSHOT

Television Stations. In the first quarter of 1998, A.H. Belo reported a pro forma (adjusted) broadcast revenue increase of 9.4%, to \$136.7 million from \$124.9 million in the first quarter of 1997. Despite particularly strong growth at the company's six CBS affiliates (Houston, New Orleans, Tulsa, Spokane, St. Louis, and

San Antonio), we believe it still recorded solid growth at its NBC and ABC affiliates. Out of the \$11.8 million increase in revenue for the quarter, \$9 million can be identified as Olympic dollars, with \$5 million of that amount being true incremental revenue. By our estimates, the company posted revenue growth of 11%, 8%, and 5% at its CBS, NBC, and ABC affiliates, respectively. At the company's two Fox affiliates, we estimate that revenues decreased by low-single digits. In our view, the company's solid growth at the NBC and ABC affiliates illustrates the importance of owning and operating significant local franchises. Also in the first quarter, the company generated an estimated \$3 million in political advertising.

The television properties recorded pro forma expense growth of 7.7%, to \$88.1 million versus \$81.8 million in the same period last year. Of the \$6.3 million of cost increases for the quarter, we believe that \$1 million reflected continuing investment in the company's local marketing agreements in Seattle and Boise (which were not included in the first-quarter or second-quarter 1997 numbers) and that \$1 million reflected additional expenditures in syndicated programming and local news. At KMOV in St. Louis, the company recently launched a new early-news show (6:00 a.m.-7:00 a.m.). Not including these items, we believe core expenses rose by 5%.

Thus far in the second quarter, the company believes that pacing is solid; paces were up by 8% in April, and by mid-single digits in May. We continue to project that the broadcast group should see double-digit pro forma growth approximating 16%, reaching \$274.0 million in 1998. Much of this growth should be fueled by political advertising, for which the company has conservatively budgeted \$16 million (\$3 million of this was already spent in the first quarter of 1998). We expect the vast majority of this money to be spent in the second half of 1998.

Newspapers. Management predicted that the first quarter would prove to be the most challenging quarter of 1998 for the newspaper group. At the newspapers, adjusted revenue increased 4.4%, rising to \$190.2 million in the first quarter from \$182.2 million during the same period in 1997. We attribute this top-line performance to growth at the company's three major papers. *The Dallas Morning News'* revenues were up slightly as retail posted flattish volume growth, general advertising expanded at a low-single-digit level, and classified volume decreased slightly. We believe that classified advertising was hurt by price increases in the low-double digits and by lower help-wanted lineage. The company suspects that Dallas' full employment may be hurting the help-wanted lineage as employers try to find candidates in markets outside of Dallas. Growth at *The Press-Enterprise* in Riverside, California, was in the low-single-digit area. At the *Providence Journal-Bulletin* in Rhode Island, we believe the company recorded low-double-digit revenue increases. However, *The Dallas Morning News* represents nearly 70% of the company's newspaper revenues, and the paper's trends steer the group's results.

Overall 4.4% pro forma revenue growth was not sufficient to offset increases in expenses, which expanded nearly 7%, to \$136.1 million in the first quarter from \$127.4 million in the same period a year ago. A significant portion of this was caused by increases in newsprint cost, which we believe climbed 15% during the quarter, creating a negative cost comparison of approximately \$3 million. Without this jump, expense growth would have approximated 4.5%. Adjusted OCF at the

newspaper contracted 1.2%, to \$54.0 million in the first quarter of 1998 from \$54.7 million the year earlier. In total, we believe that *The Dallas Morning News*, *The Press-Enterprise*, and *Providence Journal-Bulletin* had cash flow growth move slightly lower, slightly up, and up by double-digit rates, respectively. So far, second-quarter paces are stronger, with overall newspaper paces ahead by mid-single digits. The company believes that the newsprint environment should become progressively more benign and that second-quarter newsprint expenses should grow by 7%-8%, or half the first-quarter rate. By year-end, the company believes that newsprint prices could stabilize or perhaps even decline.

FINANCIAL OUTLOOK

Television Division. We project that Belo's television broadcasting properties can register a pro forma revenue gain of 11.7% in 1998, reaching \$649.1 million versus adjusted television revenues of \$580.9 million in 1997. This performance should be driven by improvements at the company's CBS affiliates owing to the Winter Olympics and to increases in political advertising spending and local ad volume. The company recorded more than \$19 million in political ad spending in the fourth quarter of 1996 alone (the company has conservatively estimated \$16 million in political advertising for 1998). Given the prowess of its local TV franchises, we think Belo can enjoy a disproportionate share of political dollars spent in its markets. The television station division's operating cash flow could climb more than 16%, to \$274.0 million in 1998, reflecting stringent cost controls.

Newspaper Division. We forecast that newspaper revenues can increase 8% for the year, climbing to \$831.3 million from a pro forma level of \$770.0 million in 1997. We expect results to be buoyed by strong and/or straightening local economies in Dallas, Riverside, and Providence. Our original projections were higher on a top-line basis for the newspaper division, but help-wanted lineage at *The Dallas Morning News* was erratic in first quarter of 1998, mainly because the unemployment rate in Dallas is so low that local employers are seeking candidates outside the market for jobs. We expect newspaper OCF to expand by approximately 11.2%, to \$244.1 million in 1998, as costs are not expected to rise as fast as revenues. We had originally forecast that newsprint prices would increase by approximately 15%, as world demand for newsprint was strong at the beginning of the year. However, demand appears to have weakened due to the Asian crisis, which should help publishers. We now estimate that newsprint costs could rise by 7.5% for the year, only half of our original projection of 15.0%.

In 1999, the company's broadcast television group could generate OCF of roughly \$291.1 million (a 6.3% gain), and the newspaper group could post OCF of \$261.7 million (assuming a relatively benign newsprint environment), up 7.2%. We also project that the company can generate free cash flow of \$110-\$115 million in 1998 and that year-end debt levels should approach \$1.5 billion. In 1999, free cash flow could reach \$153 million, and net debt should be close to \$1.37 billion at year-end.

Exhibit 51. A.H. Belo Corporation — Television Properties

Market	Market Rank	Station	Affiliation	Channel Frequency	1996	1996 Gross	1996	Share	Oversell(2)
					In-Market Viewership Share(1) (%)	Market Revenues (\$ MM)	Station Ad Revenues (\$ MM)		
Dallas-Ft. Worth	8	WFAA	ABC	8/VHF	22	\$464	\$108	23	1.1
Houston	11	KHOU	CBS	11/VHF	19	\$403	\$79	20	1.0
Seattle	12	KING	NBC	5/VHF	31	\$284	\$84	30	1.0
Sacramento, CA	20	KXTV	ABC	10/VHF	19	\$194	\$36	19	1.0
St. Louis	21	KMOV	CBS	4/VHF	23	\$201	\$40	20	0.9
Portland, OR	24	KGW	NBC	8/VHF	30	\$156	\$37	24	0.8
Charlotte, NC	28	WCNC	NBC	36/UHF	18	\$147	\$17	12	0.6
San Antonio	38	KENS	CBS	5/UHF	18	\$122	\$23	19	1.0
Norfolk, VA	39	WVEC	ABC	13/VHF	26	\$92	\$22	24	0.9
New Orleans	41	WWL	CBS	4/VHF	39	\$111	\$40	36	0.9
Albuquerque, NM	48	KASA	FOX	2/VHF	12	\$83	\$13	16	1.3
Louisville, KY	50	WHAS	ABC	11/VHF	28	\$91	\$27	30	1.1
Tulsa, OK	58	KOTV	CBS	6/VHF	29	\$71	\$20	28	1.0
Honolulu	71	KHNL	NBC	13/VHF	18	\$65	\$12	18	1.0
Spokane, WA	73	KREM	CBS	2/VHF	28	\$48	\$14	29	1.0
Tucson	78	KMSB	FOX	11/VHF	12	\$54	\$9	17	1.4
Boise, ID	125	KTVB	NBC	7/VHF	45	\$29	\$12	41	0.9

(1) In-Market Viewership Share equals a television station's viewership share divided by total of viewership shares for all commercial television stations.

(2) Oversell is the ratio of station revenue share to "in-market" audience share.

Note: Station List is Representative of All Announced Acquisitions and/or Dispositions.

Source: BIA Investing in Television '97; Nielsen Media Research; Bear, Stearns & Co. Inc.

Exhibit 52. Television Properties Managed Through Local Marketing Agreements by A.H. Belo Corporation

Market	Market Rank	Station	Affiliation	Channel Frequency	1996	1996 Gross	1996	Share	Oversell(2)
					In-Market Viewership Share(1) (%)	Market Revenues (\$ MM)	Station Ad Revenues (\$ MM)		
Seattle	12	KONG	IND	16/UHF	0	\$284	\$0	0	NA
Honolulu	71	KFVE	UPN	5/VHF	8	\$65	\$3	4	0.5
Spokane, WA	73	KSKN	UPN	22/UHF	0	\$48	\$0	0	NA
Tucson	78	KTTU	UPN	18/UHF	6	\$54	\$4	7	1.2

(1) In-Market Viewership Share equals a television station's viewership share divided by total of viewership shares for all commercial television stations.

(2) Oversell is the ratio of station revenue share to "in-market" audience share.

Note: Station List is Representative of All Announced Acquisitions and/or Dispositions

Source: BIA Investing in Television; company reports.

Exhibit 53. A.H. Belo Corporation Combined Operating Cash Flow and Income Statement — Quarterly 1997 and 1998

	1Q 1997	2Q 1997	3Q 1997	4Q 1997	FY 1997	1Q 1998	2Q 1998E	3Q 1998E	4Q 1998E	FY1998E
Dollars in Millions (Except per Share)										
Net Newspaper Revenues	\$137.2	\$171.4	\$183.0	\$202.3	\$693.8	\$190.2	\$192.9	\$213.7	\$234.5	\$831.3
Net Broadcasting Revenues	\$92.0	\$152.2	\$133.0	\$159.6	\$536.7	\$136.7	\$170.2	\$159.1	\$183.1	\$649.1
Net Other Revenues	\$3.5	\$8.3	\$3.1	\$2.9	\$17.9	\$2.6	\$3.1	\$2.1	\$3.1	\$12.0
Total Net Revenues	\$232.7	\$331.8	\$319.1	\$364.8	\$1,248.4	\$329.5	\$366.2	\$375.0	\$420.8	\$1,492.4
Operating Expenses - Newspaper	(\$90.1)	(\$118.3)	(\$132.3)	(\$146.6)	(\$487.3)	(\$136.1)	(\$132.2)	(\$151.0)	(\$168.0)	(\$587.2)
Operating Expenses - Broadcasting	(\$60.6)	(\$84.1)	(\$84.0)	(\$91.4)	(\$320.1)	(\$88.1)	(\$93.8)	(\$96.1)	(\$97.2)	(\$375.2)
Operating Expenses - Other	(\$4.8)	(\$13.3)	(\$4.5)	(\$4.5)	(\$27.1)	(\$3.9)	(\$5.0)	(\$5.0)	(\$5.0)	(\$18.9)
Total Operating Expenses	(\$155.5)	(\$215.8)	(\$220.8)	(\$242.5)	(\$834.5)	(\$228.2)	(\$231.0)	(\$252.0)	(\$270.2)	(\$981.4)
Cash Flow - Newspaper	\$47.1	\$53.0	\$50.6	\$55.7	\$206.4	\$54.0	\$60.8	\$62.8	\$66.5	\$244.1
Cash Flow - Broadcasting	\$31.4	\$68.1	\$48.9	\$68.2	\$216.7	\$48.6	\$76.3	\$63.0	\$85.9	\$273.9
Cash Flow - Other	(\$1.3)	(\$5.1)	(\$1.3)	(\$1.6)	(\$9.2)	(\$1.4)	(\$1.9)	(\$1.9)	(\$1.9)	(\$7.0)
"Broadcast" Cash Flow	\$77.2	\$116.1	\$98.2	\$122.3	\$413.9	\$101.3	\$135.2	\$123.9	\$150.6	\$511.0
Corporate Overhead	(\$6.5)	(\$8.9)	(\$9.3)	(\$13.4)	(\$38.1)	(\$9.6)	(\$10.0)	(\$10.0)	(\$10.0)	(\$39.6)
Operating Cash Flow (EBITDA)	\$70.8	\$107.2	\$88.9	\$108.9	\$375.8	\$91.7	\$125.2	\$113.9	\$140.6	\$471.4
Less: Depreciation	(\$14.4)	(\$19.5)	(\$19.0)	(\$20.3)	(\$73.1)	(\$21.4)	(\$21.3)	(\$21.3)	(\$21.3)	(\$85.2)
Less: Amortization	(\$9.0)	(\$17.0)	(\$17.8)	(\$18.1)	(\$61.9)	(\$18.6)	(\$18.8)	(\$18.8)	(\$18.8)	(\$74.9)
Less: Restructuring Charges	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0
Operating Income	\$47.5	\$70.7	\$52.1	\$70.5	\$240.8	\$51.6	\$85.2	\$73.9	\$100.6	\$311.3
Interest Expense	(\$13.4)	(\$22.9)	(\$26.9)	(\$27.6)	(\$90.8)	(\$27.2)	(\$26.9)	(\$26.6)	(\$26.3)	(\$106.9)
Other Income (Expense)	\$0.8	\$2.4	\$1.0	(\$0.5)	\$3.7	\$1.3	(\$1.1)	(\$1.1)	(\$1.1)	(\$2.0)
Pre-tax Income before Unusual Items	\$34.8	\$50.2	\$26.2	\$42.5	\$153.7	\$25.6	\$57.2	\$46.3	\$73.2	\$202.4
Taxes - Federal and State	(\$17.5)	(\$23.9)	(\$11.2)	(\$18.4)	(\$71.0)	(\$12.0)	(\$26.9)	(\$21.7)	(\$34.4)	(\$95.1)
Income/Loss before Extraordinary Items, net of Tax	\$17.4	\$26.3	\$15.0	\$24.1	\$82.7	\$13.6	\$30.3	\$24.5	\$38.8	\$107.3
Extraordinary Items										
Extraordinary (Loss)/Gain	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0
Sale of Property, net of Taxes	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0
Cum. Effect of Change in Accounting Principle	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0
Net Income (Loss)	\$17.4	\$26.3	\$15.0	\$24.1	\$82.7	\$13.6	\$30.3	\$24.5	\$38.8	\$107.3
Preferred Dividends	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0
Net Income/Loss Applicable to Common	\$17.6	\$26.3	\$15.0	\$24.1	\$82.7	\$13.6	\$30.3	\$24.5	\$38.8	\$107.3
Statistics										
Margins (Percent of Net Revenues)	1Q 1997	2Q 1997	3Q 1997	4Q 1997	FY 1997	1Q 1998	2Q 1998	3Q 1998	4Q 1998	FY1998E
Newspaper	34.3%	31.0%	27.7%	27.5%	29.8%	28.4%	31.5%	29.4%	28.4%	29.4%
Broadcasting	34.2%	44.7%	36.8%	42.7%	40.4%	35.6%	44.9%	39.6%	46.9%	42.2%
"Broadcast" Cash Flow	33.2%	35.0%	30.8%	33.5%	33.2%	30.7%	36.9%	33.0%	35.8%	34.2%
Corporate Overhead	2.8%	2.7%	2.9%	3.7%	3.1%	2.9%	2.7%	2.7%	2.4%	2.7%
Operating Cash Flow	30.4%	32.3%	27.9%	29.9%	30.1%	27.8%	34.2%	30.3%	33.4%	31.6%
Growth Rates										
Newspaper Revenue	18.4%	40.8%	50.5%	57.9%	42.4%	38.6%	12.6%	16.8%	15.9%	19.8%
Newspaper Expenses	2.0%	32.0%	49.3%	58.5%	35.7%	51.1%	11.7%	14.1%	14.6%	20.5%
Newspaper Cash Flow	70.8%	65.6%	53.8%	56.4%	61.1%	14.8%	14.6%	23.9%	19.5%	18.2%
Television Revenue	30.3%	68.4%	66.6%	72.3%	61.0%	48.6%	11.8%	19.7%	14.8%	20.9%
Television Expenses	20.2%	58.9%	57.2%	69.9%	52.0%	45.4%	11.5%	14.3%	6.4%	17.2%
Television Cash Flow	55.5%	81.7%	85.7%	75.8%	76.4%	54.7%	12.1%	28.8%	26.0%	26.4%
"Broadcast" Cash Flow	65.1%	66.9%	65.9%	64.5%	65.6%	31.1%	16.5%	26.1%	23.1%	23.5%
Operating Cash Flow	66.6%	66.2%	69.5%	52.6%	62.8%	29.5%	16.8%	28.1%	29.1%	25.4%
Shares/Per Share										
Average Outstanding Shares	45.9	62.5	62.9	63.0	58.6	63.4	63.4	63.4	63.4	63.4
EPS (Average Shares) - Before Extraordinary	\$0.38	\$0.42	\$0.24	\$0.38	\$1.41	\$0.22	\$0.48	\$0.39	\$0.61	\$1.69
EPS (Average Shares) - After Extraordinary	\$0.38	\$0.42	\$0.24	\$0.38	\$1.41	\$0.22	\$0.48	\$0.39	\$0.61	\$1.69

Source: Bear, Stearns & Co. Inc.

Exhibit 54. A.H. Belo Corporation Combined Pro Forma Operating Cash Flow and Income Statement — Quarterly 1997 and 1998

Dollars in Millions (Except per Share)	1Q 1997	2Q 1997	3Q 1997	4Q 1997	1997	1Q 1998	2Q 1998	3Q 1998	4Q 1998	1998
Net Newspaper Revenues	\$182.2	\$194.8	\$190.7	\$202.3	\$770.0	\$190.2	\$192.9	\$213.7	\$234.5	\$831.3
Net Broadcasting Revenues	\$124.9	\$155.8	\$139.5	\$160.7	\$580.9	\$136.7	\$170.2	\$159.1	\$183.1	\$649.1
Net Other Revenues	\$2.5	\$2.4	\$2.1	\$2.9	\$9.9	\$2.6	\$3.1	\$3.1	\$3.1	\$12.0
Total Net Revenues	\$309.6	\$353.0	\$332.3	\$365.9	\$1,360.8	\$329.5	\$366.2	\$376.0	\$420.8	\$1,492.4
Operating Expenses - Newspaper	(\$127.4)	(\$136.4)	(\$138.5)	(\$148.0)	(\$487.3)	(\$136.1)	(\$132.2)	(\$151.0)	(\$168.0)	(\$587.2)
Operating Expenses - Broadcasting	(\$81.8)	(\$84.2)	(\$87.6)	(\$91.9)	(\$320.1)	(\$88.1)	(\$93.8)	(\$96.1)	(\$97.2)	(\$375.2)
Operating Expenses - Other	(\$3.2)	(\$3.1)	(\$3.3)	(\$4.5)	(\$27.1)	(\$3.9)	(\$5.0)	(\$5.0)	(\$5.0)	(\$18.9)
Total Operating Expenses	(\$155.5)	(\$215.8)	(\$220.8)	(\$242.5)	(\$834.5)	(\$228.2)	(\$231.0)	(\$252.0)	(\$270.2)	(\$981.4)
Cash Flow - Newspaper	\$54.7	\$58.3	\$52.2	\$54.3	\$219.6	\$54.0	\$60.8	\$62.8	\$66.5	\$244.1
Cash Flow - Broadcasting	\$43.1	\$71.6	\$51.8	\$68.8	\$235.4	\$48.6	\$76.3	\$63.0	\$85.9	\$273.9
Cash Flow - Other	(\$0.7)	(\$0.7)	(\$1.2)	(\$1.6)	(\$4.2)	(\$1.4)	(\$1.9)	(\$1.9)	(\$1.9)	(\$7.0)
"Broadcast" Cash Flow	\$97.2	\$129.2	\$102.9	\$121.6	\$450.8	\$101.3	\$135.2	\$123.9	\$150.6	\$511.0
Corporate Overhead	(\$8.7)	(\$9.8)	(\$9.8)	(\$12.1)	(\$40.3)	(\$9.6)	(\$10.0)	(\$10.0)	(\$10.0)	(\$39.6)
Operating Cash Flow (EBITDA)	\$88.5	\$119.4	\$93.1	\$109.5	\$410.5	\$91.7	\$125.2	\$113.9	\$140.6	\$471.4
Statistics										
Margins (Percent of Net Revenues)	1Q 1997	2Q 1997	3Q 1997	4Q 1997	FY1997	1Q 1998	2Q 1998	3Q 1998	4Q 1998	FY1998
Newspaper	30.0%	29.9%	27.4%	26.9%	28.5%	28.4%	31.5%	29.4%	28.4%	29.4%
Broadcasting	34.5%	46.0%	37.2%	42.8%	40.5%	35.6%	44.9%	39.6%	46.9%	42.2%
"Broadcast" Cash Flow	31.4%	36.6%	31.0%	33.2%	33.1%	30.7%	36.9%	33.0%	35.8%	34.2%
Corporate Overhead	2.8%	2.8%	2.9%	3.3%	3.0%	2.9%	2.7%	2.7%	2.4%	2.7%
Operating Cash Flow	28.6%	33.8%	28.0%	29.9%	30.2%	27.8%	34.2%	30.3%	33.4%	31.6%
Growth Rates										
Newspaper Revenue	NA	NA	NA	NA	NA	4.4%	-0.9%	12.0%	15.9%	8.0%
Newspaper Expenses	NA	NA	NA	NA	NA	6.8%	-3.1%	9.0%	13.5%	20.5%
Newspaper Cash Flow	NA	NA	NA	NA	NA	-1.2%	4.2%	20.2%	22.4%	11.2%
Television Revenue	NA	NA	NA	NA	NA	9.4%	9.2%	14.1%	13.9%	11.7%
Television Expenses	NA	NA	NA	NA	NA	7.7%	11.4%	9.6%	5.7%	17.2%
Television Cash Flow	NA	NA	NA	NA	NA	12.7%	6.6%	21.6%	24.9%	16.4%
"Broadcast" Cash Flow	NA	NA	NA	NA	NA	4.3%	4.7%	20.5%	23.9%	13.4%
Operating Cash Flow	NA	NA	NA	NA	NA	3.6%	4.8%	22.4%	28.4%	14.8%

Source: Bear, Stearns & Co. Inc.

Exhibit 55. A.H. Belo Corporation Combined Operating Cash Flow and Income Statement — 1996-99E

	FY1996	FY1997	FY1998E	FY1999E
Dollars in Millions (Except per Share)				
Net Newspaper Revenues	\$487.2	\$693.8	\$831.3	\$871.5
Net Broadcasting Revenues	\$333.4	\$536.7	\$649.1	\$681.4
Net Other Revenues	\$3.7	\$17.9	\$12.0	\$17.5
Total Net Revenues	\$824.3	\$1,248.4	\$1,492.4	\$1,570.4
Operating Expenses - Newspaper	(\$359.1)	(\$487.3)	(\$587.2)	(\$609.8)
Operating Expenses - Broadcasting	(\$210.6)	(\$320.1)	(\$375.2)	(\$390.3)
Operating Expenses - Other	(\$4.7)	(\$27.1)	(\$18.9)	(\$21.0)
Total Operating Expenses	(\$574.4)	(\$834.5)	(\$981.4)	(\$1,021.1)
Cash Flow - Newspaper	\$128.1	\$206.4	\$244.1	\$261.7
Cash Flow - Broadcasting	\$122.8	\$216.7	\$273.9	\$291.1
Cash Flow - Other	(\$1.0)	(\$9.2)	(\$7.0)	(\$3.5)
"Broadcast" Cash Flow	\$249.9	\$413.9	\$511.0	\$549.3
Corporate Overhead	(\$19.1)	(\$38.1)	(\$39.6)	(\$33.0)
Operating Cash Flow (EBITDA)	\$230.8	\$375.8	\$471.4	\$516.3
Less: Depreciation	(\$45.4)	(\$73.1)	(\$85.2)	(\$85.0)
Less: Amortization	(\$19.8)	(\$61.9)	(\$74.9)	(\$75.0)
Less: Restructuring Charges	\$0.0	\$0.0	\$0.0	\$0.0
Operating Income	\$165.6	\$240.8	\$311.3	\$356.3
Interest Expense	(\$27.6)	(\$90.8)	(\$106.9)	(\$100.4)
Other Income (Expense)	\$6.0	\$3.7	(\$2.0)	\$4.5
Pre-tax Income before Unusual Items	\$144.0	\$153.7	\$202.4	\$260.4
Taxes - Federal and State	(\$56.5)	(\$71.0)	(\$95.1)	(\$122.4)
Income/Loss before Extraordinary Items, net of Tax	\$87.5	\$82.7	\$107.3	\$138.0
Extraordinary Items				
Extraordinary (Loss)/Gain	\$0.0	\$0.0	\$0.0	\$0.0
Sale of Property, net of Taxes	\$0.0	\$0.0	\$0.0	\$0.0
Cum. Effect of Change in Accting Principle	\$0.0	\$0.0	\$0.0	\$0.0
Net Income (Loss)	\$87.5	\$82.7	\$107.3	\$138.0
Preferred Dividends	\$0.0	\$0.0	\$0.0	\$0.0
Minority Interest				
Net Income/Loss Applicable to Common	\$87.5	\$82.7	\$107.3	\$138.0
Statistics				
Margins (Percent of Net Revenues)	FY1996	FY1997	FY1998E	FY1999E
Newspaper	26.3%	29.8%	29.4%	30.0%
Broadcasting	36.8%	40.4%	42.2%	42.7%
"Broadcast" Cash Flow	30.3%	33.2%	34.2%	35.0%
Corporate Overhead	2.3%	3.1%	2.7%	2.1%
Operating Cash Flow	28.0%	30.1%	31.6%	32.9%
Growth Rates				
Newspaper Revenue	19.1%	42.4%	19.8%	4.8%
Newspaper Expenses	12.9%	35.7%	20.5%	3.8%
Newspaper Cash Flow	40.9%	61.1%	18.2%	7.2%
Television Revenue	3.3%	61.0%	20.9%	5.0%
Television Expenses	4.8%	52.0%	17.2%	4.0%
Television Cash Flow	0.9%	76.4%	26.4%	6.3%
"Broadcast" Cash Flow	19.8%	65.6%	23.5%	7.5%
Operating Cash Flow	17.8%	62.8%	25.4%	9.5%
Shares/Per Share				
Average Outstanding Shares for EPS Calculation	41.5	58.6	63.4	63.4
EPS (Average Shares) - Before Extraordinary Items	\$2.11	\$1.41	\$1.69	\$2.18
EPS (Average Shares) - After Extraordinary Items	\$2.11	\$1.41	\$1.69	\$2.18

Source: Bear, Stearns & Co. Inc.

Exhibit 56. A.H. Belo Corporation Cash Flow Statement — 1997-99E

	FY1997	FY1998E	FY1999E
Dollars in Millions (Except per Share)			
<u>Income Statement Flows</u>			
Operating Cash Flow	\$375.8	\$471.4	\$516.3
Plus/(Minus) Other Income	3.7	(2.0)	4.5
Less: Interest Paid	(90.8)	(106.9)	(100.4)
Less: Taxes Paid	(71.0)	(95.1)	(122.4)
Dividends Paid	<u>(24.4)</u>	<u>(27.9)</u>	<u>(27.9)</u>
Net Income Statement Flows	193.3	239.5	270.1
<u>Balance Sheet Flows</u>			
Working investment	34.2	(12.5)	(12.5)
Capital Expenditures	<u>(83.3)</u>	<u>(115.0)</u>	<u>(105.0)</u>
Balance Sheet Flows - Maintenance	(49.1)	(127.5)	(117.5)
Free Cash Flow from Core Operations	144.2	112.0	152.6
<u>Acquisition/Sale of Television Properties</u>			
Newspaper/Station Acquisitions	0.0	0.0	0.0
Providence Journal Acquisition	(587.0)	0.0	0.0
Press-Enterprise and Others	(165.1)	0.0	0.0
TVFN Exchange	(75.0)	0.0	0.0
Sale of GemStar Shares (243M @ \$24)	5.8	0.0	0.0
Asset Dispositions	0.0	0.0	0.0
Other	1.1	0.0	0.0
Less: Taxes Paid on Gain of TVFN	0.0	(30.0)	0.0
Closing Costs/Transaction Fees	<u>(117.4)</u>	<u>0.0</u>	<u>0.0</u>
Acquisition/Sale of Television Properties	(937.5)	(30.0)	0.0
<u>Financing Activities</u>			
Borrowed/(Applied) from/ to Revolver	0.0	0.0	0.0
Senior Debt Raised	1,100.5	0.0	0.0
Senior Debt Repurchased	0.0	0.0	0.0
Refinancing of Providence Journal debt	(200.0)	0.0	0.0
Net proceeds from fixed-rate debt offerings	990.0	0.0	0.0
New Public Equity Raised - Net Proceeds	0.0	0.0	0.0
Share Repurchases	0.0	0.0	0.0
Applied to Revolver Repayment	(1,111.0)	(75.0)	(125.0)
Proceeds from Exercise of Stock Options	<u>11.9</u>	<u>0.0</u>	<u>0.0</u>
Financing Activities	791.4	(75.0)	(125.0)
Net Increase/(Decrease) in Cash	(1.9)	7.0	27.6
<u>Statistics:</u>			
<u>Free Cash Flow per Average Share</u>			
FCF from Operations per Share	\$2.46	\$1.77	\$2.41
<u>Net Debt</u>			
Cash - Year-End	\$11.9	\$18.9	\$46.5
Projected Debt - Year-End	\$1,614.0	\$1,539.0	\$1,414.0
Projected Net Debt - Year-End	\$1,602.1	\$1,520.1	\$1,367.5
<u>Leverage</u>			
Leverage - Net Debt - Pro Forma OCF	4.3	3.2	2.6

Source: Bear, Stearns & Co. Inc.

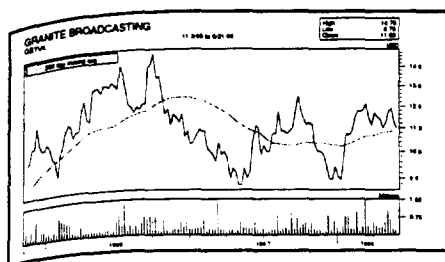
Exhibit 57. A. H. Belo Corporation Valuation Using Discounted Cash Flow Analysis

<u>Calculation of Cash Flows for Valuation Purposes</u>		<u>1999E</u>	<u>2000E</u>	<u>2001E</u>
Pre-Tax Income		\$260.4	\$335.3	\$395.4
Adjustment for Pro-forma Cash Flow				
Plus: Interest Expense		\$100.4	\$92.3	\$87.8
Unlevered Pre-Tax Income		\$360.8	\$427.5	\$483.2
Taxes at Rate of	40.0%	(\$144.3)	(\$171.0)	(\$193.3)
Unlevered Net Income		\$216.5	\$256.5	\$289.9
Non-Cash Expenses		\$160.0	\$160.0	\$160.0
Firm Payments		\$0.0	\$0.0	\$0.0
Working Capital Investment		(\$12.5)	(\$12.5)	(\$12.5)
Capital Expenditures		(\$105.0)	(\$105.0)	(\$80.0)
Unlevered Free Cash Flow from Operations		\$259.0	\$299.0	\$357.4
Terminal Value of FCF Assuming Perpetual Growth Rate of	6.0%			\$7,553.4
Cash Flows for Valuation Purposes		\$259.0	\$299.0	\$7,910.8
<u>Equity Value</u>				
Enterprise Value (NPV) Using Discount Rate of	11.0%	\$6,947.1		
Debt Outstanding - Year End (1998 Pro Forma)		(\$1,539.0)		
Cash - Beginning of Year		\$18.9		
Equity Value		\$5,427.0		
<u>Share Price</u>				
Shares - Fully Diluted		63.8		
Private Market Value - Target Price		\$85.01		
"Hidden Assets"		\$1.82		
PMV plus Hidden Assets		\$86.83		
Discount Applied to PMV		20.0%		
Target Stock Price		\$69.47		
Current Share Price		\$53.06		
Upside to Target		30.9%		

Source: Bear, Stearns & Co. Inc.

GRANITE BROADCASTING, INC. (GBTVK-11)

Rating: Buy



52-Week Range

\$13-\$8 1/2

EPS

12/97: (\$2.93)

12/98E: (\$3.20)

12/99E: (\$2.44)

P/E

12/98E: NM

12/99E: NM

BCF (mil)

12/97PFE: \$67.2

12/98PFE: \$73.5

12/99PFE: \$82.2

EV/BCF

12/98PFE: 11.0x

12/99PFE: 9.8x

Dividend

Nil

Yield

Nil

Com. Shares (mil)

18.4

Equity Market Capitalization (mil)

\$202

Total Debt/EBITDA (1998E)

9.1x

Est. 3-Yr BCF Growth Rate

11.1%

Motown Momentum, Big Bets on WB — And Trading at a Fraction of Private Market Value

On January 13, 1998, we raised our rating on Granite Broadcasting to Buy from Attractive, at an opening price of \$10 3/8. Our ongoing enthusiasm stems from the company's new strategic direction over the past year, which has placed a greater emphasis on the purchase of stations affiliated with the emerging WB network in large metropolitan markets, as exemplified by its 1997 acquisitions of WDWB in Detroit and KOFY in San Francisco. Moreover, with the recent sale of television properties in Grand Rapids and Lansing, Michigan (which it did to help finance the recent acquisitions), the company has improved its financial flexibility, which we consider key to any broadcaster's ability to play the positive trends unfolding in the broadcast TV business over the next few years. We believe that Granite can register average pro forma BCF growth of 9.4% in 1998 and 11.8% in 1999.

We think that these positive factors more than offset concerns we have about the company's excessive leverage, the untested nature of its new strategic charter, and the possibility that it may not be able to obtain a waiver from the FCC to own TV properties in San Francisco and Monterey/Salinas/San Jose, which would diminish the favorable economics of the San Francisco station.

- Compelling Valuation.** By our calculations, the market is currently valuing Granite's core stations at 8.9x the company's projected 1998 BCF estimate, which we consider unduly low given the company's growth potential. Applying a multiple of 10.75x to our 1999 BCF estimate of \$82.2 million and adjust for debt and exchangeable preferred stock, we arrive at a 12-month target price of \$15 per share for GBTVK. The stock is also selling at a fraction of its private market value, which we peg at \$20 or more.
- Strategic Shift Brightens Long-Term Potential.** With its recent purchases of WDWB in Detroit (February 1997) and KOFY in San Francisco (October 1997), Granite now delivers 4.2% of total TV households for the WB network and ranks as the network's second-largest affiliate in terms of clearance (after Tribune, which has in excess of 26% of the network's coverage). Through the purchase of KOFY, Granite catapulted itself from its position as the 31st-largest broadcaster (in terms of clearance) to the 18th largest. We view this shift as a reflection of management's growing belief in the importance of scale (especially in large metro markets) in helping

TV broadcasters to secure the highest-quality, most popular programming. Moreover, the company's stations will now participate in markets that collectively generate \$1.5 billion in TV advertising revenues.

- **A Major Bet on WB.** We think this new strategic shift can pay big dividends, especially if Granite can get promotion and programming support from the WB network's co-owners, Time Warner and Tribune. The broadcaster expects its WB stations in Detroit and San Francisco to participate in the ongoing success of the WB network (in terms of improved ratings and image) over the next few years, particularly given the network's rollout of Tuesday night programming in 1998 (already accomplished) and of Thursday night programming in 1999.
- **Dancing in Motown.** After a slow start, it appears that Granite's WDWB station in Detroit is showing signs of strength. Management has invested in programming, marketing, and promotion to give the station a greater presence in the marketplace and has replaced management in key positions. These measures appear to be paying off (pacings ran at a low-double-digit pace in the first quarter of 1998, and this momentum has carried into the second quarter). We project that WDWB can record an 18% increase in BCF in 1998.
- **KOFY Time in San Francisco.** Granite believes that KOFY could become its single-largest revenue and cash flow contributor in the television station group as it strives to improve its programming (by launching local news), rides the continuing success of the WB network, takes greater advantage of the strong San Francisco advertising market and cross-promotion/selling opportunities with the nearby KNTV in San Jose (which it hopes to serve with a cross-ownership waiver from the FCC), and continues to cut costs. Management hopes to close on the purchase in July and forecasts that the station can generate BCF of \$13 million in 1999. In our view, this station has the potential to produce annual BCF in the \$20-\$30 million range over the long term.

**VALUATION: TRADING
AT A FRACTION OF ITS
PRIVATE MARKET
VALUE**

By our calculations, the most recent transactions in the broadcast television industry have been made at 12.0x-14.0x 12-month forward broadcast cash flow. Applying these multiples to GBTVK would yield values of \$16¹/₂-\$24, implying that the company's stock is trading at a 50%-72% discount to its private market value. The gap seems excessively wide, in our opinion.

On a fully diluted basis, Granite's equity capitalization approximates \$202.4 million. Factoring in pro forma net debt — expected to reach \$412.5 million in 1998 — and the payment-in-kind (PIK) preferred stock accruing to an estimated \$190 million, the company's total enterprise value comes to \$804.9 million. If we then subtract the purchase prices of Detroit (\$175.0 million) and San Francisco (\$173.75 million), assuming that the company paid full price for these stations, we arrive at an implied

value of \$456.2 million for Granite's core, non-WB stations. Assuming that pro forma BCF for the company is \$73.5 million and that the expected cash flow of the Detroit and San Francisco stations could approximate \$20 million in 1998, core station cash flow should total \$53.5 million. Based on the figures above, the market is valuing the company's core stations at 8.5x 1998 BCF (\$456.2 million divided by \$53.5 million). Once again, we consider this valuation unduly low.

Could it be that Granite paid too much for the San Francisco and Detroit stations, thereby understating the value of the core operations? We think not. If, for example, we assumed that the core stations were valued at 9.5x, then the implied amount by which the company "overpaid" for the two WB affiliates would approximate \$67 million, implying that a more reasonable purchase price would have been \$281.75 million. Judging from recent transactions, we do not believe it would be possible for any company to buy these stations in San Francisco and Detroit so cheaply. Hence, looking at Granite's current valuation from both angles — i.e., the implied multiple of the core stations (8.2x) or the implied amount by which the company overpaid — it appears as though the stock is attractively valued at current prices.

If we apply a 10.75x multiple to our 1999 BCF estimate of \$82.2 million for the core stations (which reflects the growth potential of the company's WB affiliates) Granite's total enterprise value would approach \$883.7 million. After adjusting for debt and exchangeable preferred stock, the equity value comes to roughly \$278.5 million, or \$15 per share. Recent sales of television stations have been consummated at 12x-14x 12-month forward BCF. On this basis, Granite would be worth \$20 (using the midpoint of the takeout range on recent transactions, or 13x).

PLACING LARGE BETS ON THE WB NETWORK

We believe that an essential component of Granite's growth strategy is its emphasis on larger-market, faster-growing WB affiliates, which it launched with the purchase of WDWB in Detroit and culminated with the announced acquisition of KOFY, a WB affiliate in San Francisco. This marks a dramatic shift from only a year ago, when the company's focus appeared to be more on acquiring dominant middle-market network-affiliated TV stations, then working to bolster the revenues and profitability by improving the news products. With the two recent acquisitions, the company also appears to have abandoned its long-standing strategy to cluster its operations in Michigan. The company's side-by-side Lansing/Grand Rapids/Detroit focus (a stated corporate objective only a year ago) has been set aside while it pursues a plan to cluster stations in San Francisco and in the Salinas/Monterey/San Jose community.

Granite has purchased the only two top ten WB affiliates not owned by Tribune, a partner of the WB network. The company has spent a combined \$348.75 million on this new station strategy, purchasing WDWB for \$175.0 million and KOFY for \$173.75 million. Through the purchase of KOFY, Granite catapults itself from its position as the 31st-largest broadcaster (in terms of clearance) to the 18th largest. We think this shift is a reflection of management's growing belief in the importance of scale (especially in large metro markets) and in securing the highest-quality, most popular programming. Moreover, the company's stations will now participate in markets that collectively generate \$1.5 billion in TV advertising revenues. By delivering 4.2% of total TV households for the WB, Granite ranks as the network's

second-largest affiliate in terms of clearance (Tribune has in excess of 26% of the network's coverage). We think this should reap significant rewards, especially if Granite can obtain promotion and programming support from the network's co-owners, Time Warner and Tribune.

In order to finance this transition, Granite, balking at issuing more equity at historically low prices, opted to sell assets. On January 13, 1998, the company announced that it was selling WLAJ-TV in Lansing, Michigan (after exercising the right to buy the station for \$19.4 million), and WWMT-TV in Grand Rapids, Michigan, to Freedom Communications for \$170 million, which we believe represents sales multiples of 17.0x 1997 BCF and 13.5x 1998 BCF. The company purchased the Grand Rapids station in 1995 for \$95.0 million and has an option to purchase the Lansing station for \$19.4 million. Combined, Granite spent \$114.4 million on the two stations and is selling these properties for a \$55.6 million gain (more than 49% above the company's purchase price). With the sale of these two stations, the transition from the Big Three middle-market network-affiliated strategy gathered steam.

We believe that the company's operating risk profile has increased somewhat because Granite is essentially trading two well-established and profitable network-affiliated TV properties for two emerging WB affiliates, which had been owned by entrepreneurs and currently have a very low profile in their respective markets. The CBS-affiliated Grand Rapids station captured 30% of "in-market" local viewership share, while the ABC affiliated Lansing station commanded a 14% in-market share. More than 50% of Granite's total coverage will now be associated with WB affiliates in the top ten markets.

Granite believes that the developing WB network offers the best growth opportunities to broadcast television as the network continues to roll out more nighttime programming (it added Tuesday night in 1998 and is expected to launch Friday night programming in 1999). Granite expects the WB stations in Detroit and San Francisco to participate in the improved ratings and image that the network has enjoyed for the past several years. Sinclair Broadcast Group's recent vote of confidence in the network (although the WB paid for access to Sinclair's distribution network) also creates momentum for the network.

In the 1996-97 broadcast season that ended in May, the WB network showed the most growth and was up nearly 6% in terms of households. This compares favorably with NBC (which was down 9.4%), CBS (up 0.9%), ABC (down 11.9%), and UPN (up 3.1%). Through the first 28 weeks (through April 5, 1998) of the 1997-98 broadcast season, WB has demonstrated significant growth in terms of TV households, climbing 19.9%. Among adults 18-34, it rose 25.6%, while it jumped 25.9% among adults in the 25-54 age bracket. In terms of the new networks, WB has made significant gains on UPN. Through the first 28 weeks of the 1996-1997 broadcast season, UPN held a lead of nearly 50% over WB in adults aged 18-49. In the 1997-98 broadcast season, the two networks are essentially even on this measure and, in recent weeks, WB has begun to overtake UPN in terms of households and the attractive 18-49 and 25-49 demographics. During the past 12 weeks, UPN

households are down 3.9%, and the number for adults in the 18-49 age group fell 10.5%.

After the two stations are purchased, we believe that pro forma revenues will be divided fairly evenly among four networks, with ABC, CBS, NBC, and WB affiliates representing 37%, 18%, 20% and 25% of the pro forma total, respectively. In addition, no single television station should account for more than 16% of revenue (it is estimated that the Buffalo station accounts for 18% of pro forma revenue, while Grand Rapids, Detroit, San Jose, and San Francisco are all expected to deliver 10%-12% of revenues apiece).

Motown Showing Momentum

In early February 1997, Granite closed on the purchase of WDWB (formerly WXON), the WB affiliate in Detroit. We think the company had higher expectations for Detroit in 1997 than what actually transpired in the station's first 11 months under Granite's management. When Granite purchased the Detroit station, programming was weak, the sales department management was not in place, the station "repped" itself for national advertising, and margins were monumental (running 60%-plus) — a result of a particularly lean operation. Although it closed on the purchase on February 1, more than a month earlier than expected, Granite did not hire a general sales manager until June 1997 and did not have national and local sales managers until the fourth quarter. Moreover, the company invested money in programming, marketing, and promotion to boost the station's profile in the marketplace. We believe that the unfocused sales effort, combined with the rise in costs, translated into virtually flat growth, with BCF coming in roughly even with the estimated \$10-\$10.5 million earned in 1997. At this point, however, we think the new sales department is writing higher levels of business, especially in terms of national advertising. Sales at the station have been pacing ahead by low-double-digit growth for the first half of 1998, and we expect this momentum to persist.

In addition, the WB network has solid momentum. While programming is still a weakness at the station, we believe that cash flow is strengthening. We forecast that BCF can climb nearly 18%, to \$12.5 million, at the station in 1998.

KOFY Time in San Francisco

On October 6, 1997, Granite Broadcasting announced its intention to purchase the stock of Pacific FM, the owner of KOFY-TV (the WB affiliate in San Francisco, California), for \$143.75 million and entered into a five-year noncompete with Pacific FM's principal owner, Jim Gabbert, for \$30 million. By clustering in San Francisco and San Jose, Granite intends to 1) leverage KNTV's news production to quickly enter the San Francisco news market, which approximates \$150 million in revenue; 2) improve KNTV's ability to access better programming in the 122nd-largest TV market; 3) cross-promote between the two stations; and 4) create operating efficiencies between the stations.

In 1996, we estimate that KOFY-TV earned \$20-\$25 million in revenue, grabbing only 3.5%-4% of San Francisco's \$575 million advertising market. In addition, we

believe that the station earned BCF margins approaching 5%. In all, the station generated an estimated BCF of \$1-\$2 million.

Granite has identified significant revenue and expense opportunities at KOFY. While the station is expected to deliver 10%-12% of the company's pro forma 1998 revenue, Granite believes that it will eventually become the single-largest revenue and cash flow contributor of the company's station group, owing to several factors. On the revenue side, the company believes there are four opportunities.

- **Using News Programming to Grab Share.** The 1998 San Francisco TV advertising market is expected to reach \$600 million, and \$150 million of this advertising could be placed in news programming. Granite plans to use the news production capabilities at KNTV-TV in San Jose, a neighboring market with substantial signal overlap, to immediately launch a news product in San Francisco on KOFY-TV. Management estimates that this could add \$8-\$12 million in revenue within the next several years.
- **Riding the Growth of WB.** Granite should benefit from the continued expansion of the WB network, which has added Tuesday night and will add their Thursday night programming in the fall of 1998. The company believes that the additional nights could add \$2-\$3 million in incremental revenue in the next couple of years.
- **Offering Paid Programming.** The company expects to earn \$2-\$5 million in paid programming, which it does not yet run.
- **Market Gains in San Francisco.** Granite estimates that if it can get its fair share of San Francisco's 4%-6% market growth over the next several years, it could add \$2-\$5 million in incremental revenues.

On the cost side, Granite has identified \$5-\$6 million in immediate cost cuts, which should trickle down directly to the BCF line. Moreover, KNTV and KOFY should benefit from cross-promotion and save money by combining expenses. At the low end of the range, this would imply potential incremental cash flow of \$20 million or so within a few years and up to \$30 million over the long term. Granite expects to close on KOFY in July 1998 and to earn pro forma BCF of approximately \$13 million in 1999.

The purchase price of KOFY, at \$173.75 million, was significant, especially given the fact that Granite purchased KOFY for stock (it is estimated that Gabbert paid approximately \$10 million for the station in 1980). We do not think that Granite will enjoy a tax shield from the transaction. However, the company should be able to accelerate the \$30 million noncompete agreement over five years.

The largest challenge confronting the company's strategy to cluster stations in San Francisco and San Jose is the ability to secure an FCC waiver between the two stations, which have significant Grade A overlap.

MAJOR INVESTMENT CONCERNS

Is the FCC Prepared to Potentially Set a Precedent?

With the proposed purchase of KOFY, Granite petitioned the FCC for a waiver of the ownership rules to permit a Grade A overlap between the Salinas/Monterey/San Jose market (KNTV-TV) and San Francisco. We've analyzed the company's petition and believe it makes a reasonable case for the waiver, owing to the following:

- combined, the stations capture only 6% of San Francisco's advertising dollars;
- the San Jose station does not command measurable audience share in San Francisco (and vice versa),
- there are literally dozens of distinct television and radio station voices in the market; and
- the waiver would be compatible with the FCC's stated intention to support minority-owned broadcasters (the NTIA estimates that less than 3% of all broadcast properties are owned by minorities).

The major hurdle Granite will face is precedent. Is the FCC willing to create a potential Grade A duopoly policy? The petition drew only one negative response from the Chronicle Publishing Company, which asks that the decision on Granite's purchase be deferred until the commission is able to codify duopoly rules. If Granite is granted a waiver, this would be an obvious victory for the company. However, if the waiver is not granted, we expect the company to either sell or (more likely) swap the San Jose station. Because it generated \$7.5-\$8.0 million in BCF in 1997, we believe the station could be valued at \$95-\$110 million.

Company Still Has Significant Leverage

The sale of the television properties in Lansing and Grand Rapids should provide significant liquidity for the company. Because of its net operating losses (NOLs), we don't expect the company will pay taxes on the gain of the Lansing/Grand Rapids sale, and, therefore, it will net \$150.6 million in proceeds (\$170 million purchase price less purchase of Lansing station for \$19.4 million). This money will be used to fund the \$173.5 million purchase of KOFY in San Francisco. More importantly, it reduces the amount of funds the company would have had to raise to finance the KOFY purchase. If the company had not sold these two stations, we estimate that year-end 1998 pro forma leverage would have approximated 7.0x total debt, or 9.4x total debt plus cumulative exchangeable preferred stock. Selling the stations will reduce pro forma leverage to 6.2x and 9.1x, respectively.

While hardly ideal, we consider the new capital structure less unwieldy. By our estimates, Granite has the flexibility to increase its leverage to 6.5x on a debt basis and could try to address the PIK preferred stock. In May 1998, the company executed a \$175 million senior subordinated debt offering that was used to pay down senior bank debt and buy back some higher coupon debt. This issuance should also provide more borrowing capacity at the senior level, thereby possibly permitting the

company to buy back some of its PIK preferred stock, which has a high dividend rate.

FIRST-QUARTER SNAPSHOT

Granite started off 1998 with a strong first-quarter performance. Net revenues rose 13.7%, to \$36.7 million. Of the \$4.4 million increase, \$1.2 million came from operating WDWB for an extra month. Granite has been running the station since February 1, 1997. In the first quarter of 1998, reported operating expenses grew 12.7%, to \$22.3 million from \$19.8 million last year. Approximately one-third, or \$700,000 of the \$2.5 million increase in expenses, was due to an extra month of operation of WDWB in 1998. Reported BCF climbed 15.3%, to \$14.4 million, or \$1.9 million above the first-quarter 1997 BCF of \$12.5 million. Same-station revenue for the quarter rose 10.5%, to \$36.7 million versus \$33.2 million the year before. Same-station broadcast cash flow increased 12.5%, to \$14.4 million.

We believe growth was fueled by 1) continued strength at WDWB in Detroit; 2) Olympic-related advertising dollars placed for the winter games; and 3) moderate growth at the company's ABC and NBC affiliates at the local level. Considering that the company's CBS affiliates contributed only 30% of the quarter's revenue, we consider these results particularly strong. We believe local nonpolitical advertising was up approximately 13% in the quarter, with strong performance being posted by WWMT in Kalamazoo (up 30%), WPTA in Fort Wayne (up 16%), and WKBW in Buffalo (up 13%). National nonpolitical revenue for the group was up around 4%, with WWMT in Kalamazoo (up 41%), WTVH in Syracuse (up 14%), and KEYE in Austin (up 9%) leading the group. The ability to achieve revenue growth across all affiliations (CBS stations were up 20% for the quarter and the ABC and NBC affiliates' revenue expanded by mid-single digits) is a testimony to the important role the company's local stations play in their respective markets.

FINANCIAL OUTLOOK

We project that reported revenues at the television broadcasting properties can rise by roughly 8.0% in 1998, to \$165.8 million. This performance should be driven by accelerating growth at the company's WB affiliates, improvements at the CBS affiliates (thanks to the Winter Olympics), increases in political advertising spending, and higher local ad volume. BCF could climb approximately 9.2%, to \$76.2 million. On a pro forma basis, which includes KOFY and excludes the Detroit stations, we believe Granite can post \$73.5 million in BCF. In 1999, we expect that BCF could expand by nearly 11.8% on a pro forma basis, to \$82.2 million from \$73.5 million, reflecting the continued accelerated growth of the WB affiliates in San Francisco (1999 will be the first year in which the company operates the station for an entire calendar year) and Detroit as well as mid-single-digit growth at the company's core stations (aided by slower expense growth).